Recent Cases of Interest to Fiduciaries

RONALD D. AUCUTT
703 712 5497 | raucutt@mcguirewoods.com

MICHAEL H. BARKER
804 775 1679 | mbarker@mcguirewoods.com

DENNIS BELCHER
804 775 1679 | dbelcher@mcguirewoods.com

ADAM M. DAMEROW
312 849 3681 | adamerow@mcguirewoods.com

CHARLES D. FOX IV
434 977 2597 | cfox@mcguirewoods.com

MEGHAN L. G. HUBBARD
804 775 4717 | mghubbard@mcguirewoods.com

WILLIAM M. LONG
312 750 8916 | wlong@mcguirewoods.com

SCOTT W. MASSELLI
804 775 7585 | smasselli@mcguirewoods.com

SEAN F. MURPHY
703 712 5487 | sfmurphy@mcguirewoods.com

STEPHEN W. MURPHY
434 977 2538 | swmurphy@mcguirewoods.com

JOHN B. O'GRADY
804 775 1023 | jogrady@mcguirewoods.com

MARTIN A. STEIN
312 849 8191 | mstein@mcguirewoods.com

ILAN Z. WEINBERGER
202 857 2481 | iweinberger@mcguirewoods.com

July 2016
www.mcguirewoods.com

McGuireWoods marketing communications are intended to provide information of general interest to the public. Marketing communications are not intended to offer legal advice about specific situations or problems. McGuireWoods does not intend to create an attorney-client relationship by offering general interest information, and reliance on information presented in marketing communications does not create such a relationship. You should consult a lawyer if you need legal advice regarding a specific situation or problem.

Contents © 2016 McGuireWoods LLP.

Table of Contents

In the Matter of Estate of Leon C. Chamberlain, 135 A.D.3d 1052 (N.Y. App. Div. Jan. 7, 2016)........ 1

Domino v. Braswell, 165 So.3d 530 (Miss. Ct. App. May 19, 2015)........ 1

In re Estate of Tigani, No. CV 7339-ML (Del. Ch. Ct. Feb. 12, 2016)........ 3

Queen v. Schmidt, No. CV 10-2017 (PLF), 2015 WL 5175712 (D.D.C. Sept. 3, 2015)........ 5

Estate of Zucker, 122 A.3d 1112 (Pa. Super. Ct. 2015)........ 6

Gladden v. Cumberland Trust and Investment Company, 2016 WL 1166341 (Tenn. Ct. App., Mar. 24, 2016)........ 7

United States v. Lazare, 2016 WL 1127627 (D. Nev. Mar. 4, 2016)........ 8

Berlinger v. Wells Fargo, N.A., 2016 WL 740521 (M.D. Fla., Feb. 25, 2016)........ 9

Trupp v. Naughton, No. 320843, 2015 Mich. App. LEXIS 1114 (Ct. App. May 26, 2015)........ 10

Kelly v. Orr, 243 Cal. App. 4th 940 (Jan. 11, 2016)........ 12

Estate of Gilliland, No. B262482, 2016 WL 109882 (Cal. Ct. App. Jan. 8, 2016)........ 133

McDevitt v. Wellin, 2016 WL 199626 (D.S.C., Jan. 15, 2016)........ 14

In re Estate of George Mathai (2014-482, NYLJ 1202716307504, at *1 (Surrogate's Court, Jan. 7, 2015)........ 15

United States v. Read, 2016 WL 310721 (D. Conn 2016)........ 16

Schrage v. Seberger Living Trust, 2016 WL 914796 (Ct. App. Ind., March 10, 2016)........ 17

DeJohn v. Wheeler, 2016 WL 270033 (Ct. App. Cal., Jan. 21, 2016)........ 18

Monschke v. Timber Ridge Assisted Living, LLC, 244 Cal.App.4th 583 (Jan. 29, 2016)........ 19

In the Matter of Ronald J. Mount 2012 Irrevocable Dynasty Trust U/A/D Dec. 5, 2012, C.A. No. 10991–VCN, 2016 WL 297655 (Del. Ch. Jan. 21, 2016)........ 21

Robert Rauschenberg Found. v. Grutman, No. 2D14-3794, 2016 WL 56456 (Fla. Dist. Ct. App. Jan. 6, 2016), *reh'g denied* (Feb. 24, 2016), *review denied*, No. SC16-502, 2016 WL 3185202 (Fla. June 8, 2016)........ 22

Duckett v. Enomoto, No. CV-14-01771-PHX-NVW, 2016 WL 1554979 (D. Ariz. Apr. 18 2016)........ 23

In the Matter of Estate of Leon C. Chamberlain, 135 A.D.3d 1052 (N.Y. App. Div. Jan. 7, 2016)

Modification of trust terms is appropriate where limitations on investments permitted under trust instrument frustrated the purposes of the trust, even though this circumstance was not necessarily "unforeseen" at the time of creation of the trust

Facts: Leon Chamberlain died in 1999. In his will, he made bequests to three churches, to be held in trust and invested only in government securities and insured bank accounts. The income from the trusts was to be used for maintenance of the physical property of each church. The churches argued that the restrictions on the types of investments in the will rendered the trust income essentially negligible. Accordingly, the churches filed a petition, with the consent of the New York Attorney General, to amend the investment restrictions and to allow for investment in accordance with the Prudent Investor Act. The trial court denied the petition, finding that no "unforeseen" change in circumstances had occurred. The churches appealed.

Law: New York law recognizes the power of the court to modify a trust, where a change in circumstances since the execution of the instrument renders literal compliance with the instrument impossible or impracticable. First, New York recognizes equitable deviation, where an administrative provision is altered or amended. Second, New York recognizes the doctrine of *cy pres*, where a substantive change to the trust is sought, such as a change to the charitable purpose or a dispositive provision. In those circumstances, the court has statutory authority to order changes that in its judgment, will most effectively accomplish the general purposes of the trust. Some cases have held that at common law, an *unforeseen* change in circumstances is required for equitable deviation from a trust document. However, the applicable statutory provision does not expressly require the change to be unforeseen.

Holding: On appeal, the Supreme Court, Appellate Division reversed the Surrogate's Court's decision, emphasizing that the investment restrictions in the will had become impracticable and had frustrated the charitable purpose of the trust. The Court found that the additional authority that the churches sought was limited and that they did not seek to alter the specific charitable purposes or terms of disposition. The Court further noted that other courts have "cautiously exercised" their equitable powers to permit deviation from the settlor's investment restrictions in similar circumstances.

Practice Point: The absence of unforeseen circumstances does not necessarily preclude the court from exercising its authority to grant such a request. An interested party can petition the court for permission to deviate from or modify restrictions of the trust on the types of permissible investments which have subsequently frustrated the purpose of the trust.

Domino v. Braswell, 165 So.3d 530 (Miss. Ct. App. May 19, 2015)

Filing of trust as public record triggers statute of limitations

Facts: Ophelia Braswell ("Ophelia") executed a trust agreement in 1994, naming her four living children as trustees. A fifth child had previously died. The trust agreement recited that it was irrevocable and not subject to amendment, and that Ophelia would have no further right, title, or interest in the property contributed to the trust. The trust agreement further provided that upon Ophelia's death, one-fifth of the trust assets would be distributed to each of her four living children,

and one-tenth of the trust assets would be distributed to each of the two children of her fifth child who predeceased her.

Despite the provision of the trust agreement that prohibited amendment, Ophelia executed, in 1997, a modification to the trust agreement to correct an error. The amendment modified the distribution provision such that if a beneficiary predeceased Ophelia, his or her share would be distributed as the beneficiary might provide in the beneficiary's will. If the beneficiary did not exercise this power of appointment in the beneficiary's will, the beneficiary's interest would be conveyed to the beneficiary's surviving spouse and issue. This amendment was filed as a public record after its execution in 1997.

Two more of Ophelia's children, Ralph and Charles, predeceased Ophelia. After Ophelia died in 2013, a dispute arose between Ralph's widow and his children and grandchildren. There also arose another dispute between Charles's widow and his children. Ophelia's two living children filed a complaint for interpleader as co-trustees regarding Ralph's and Charles's interest in the trust. The chancery court accepted deposits of checks for Ralph's and Charles's shares and discharged the co-trustees from liability. The children moved for judgment on the pleadings, arguing that the modification to the trust agreement was void. The widows opposed this motion and filed cross-motions for judgment on the pleadings and to dismiss.

The Chancery Court foe Bolivar County found that the modification of the trust agreement was valid and that Mississippi's ten-year statute of limitations barred their claims as untimely. The Chancery Court specifically found for Charles's and Ralph's wives, holding that the trust could be modified despite the trust agreement clause to the contrary. Further, the Chancery Court found that the ten-year statute of limitations barred the children from contesting the trust modification. The Chancery Court found that the statute of limitations was triggered when the modification was filed in the public record in 1997, citing the Fifth Circuit's decisions in *Ayers v. Davidson*, where such filing was deemed "notice to all the world." The Chancery Court rejected the children's theory that the statute of limitations never began to run because the purported modification was void. The children appealed from both rulings.

Law: Mississippi law provides for a statute of limitations of ten years for trust actions.

Holding: The Mississippi Court of Appeals affirmed the Chancery Court's decision, holding that the statute of limitations began to run on the date when the trust modification was filed as a public record. The Court of Appeals declined to rule on the other issues brought on appeal, as its ruling on the statute of limitations rendered them moot.

Practice Point: A trustee or other interested party who wishes to limit claims regarding a trust or other action can explore various ways to begin the limitations period. In addition, a beneficiary or other interested party should be aware of those limitations periods, to avoid a situation in which that party's claim is unexpectedly barred by a statute of limitations. In Mississippi, a trustee can trigger the running of the statute of limitations by filing a trust document in the public record.

Under the Uniform Trust Code, now adopted in 31 states and the District of Columbia, a beneficiary may not commence a proceeding against a trustee for breach of trust more than one year after the date the beneficiary was sent a report that adequately disclosed the existence of a potential claim for breach of trust. *See* Unif. Tr. Code § 1005(a). The fact that this limitations period can commence even when the beneficiary receives a "report," rather than a formal "accounting," is not necessarily something an interested party might otherwise anticipate happening.

In re Estate of Tigani, No. CV 7339-ML (Del. Ch. Ct. Feb. 12, 2016)

A remainder beneficiary in default of exercise of testamentary limited power of appointment has standing regarding trust, and the donee of testamentary limited power of appointment may not remove the appointee's standing by contracting to exercise that power during life

Facts: In 1995, J. Vincent Tigani, Jr. executed a pour-over will, which designated his wife as executrix of his estate, and a revocable trust that designated his wife as successor trustee and beneficiary during her lifetime. The trust agreement further gave Mrs. Tigani a limited testamentary power of appointment, allowing her to appoint the trust assets remaining at her death among descendants of Mr. Tigani who survive Mrs. Tigani. Any property not appointed was to be divided equally among the Tiganis' three children. Mrs. Tigani made similar reciprocal provisions in her estate documents.

Over the following years, the relationship between Mrs. Tigani and one of the three children, Bruce, became strained. As a result, the Tiganis and their counsel discussed several variations of new estate documents that partially or fully disinherited Bruce. However, Mr. Tigani died in 2011 before his new estate documents could be executed. Mrs. Tigani then became the successor trustee and the executrix of Mr. Tigani's estate.

The day after Mr. Tigani died, Mrs. Tigani executed a new will and an amendment to her trust agreement. In her will, she purported to exercise her power of appointment by directing the trustee of Mr. Tigani's trust to distribute the trust assets to the trustee of her trust, to be administered pursuant to the amended trust agreement. In the amended trust agreement, Mrs. Tigani ordered the distribution of the bulk of the assets to her other two children and a limited distribution of one third of the Trust's "business interests" to Bruce. The relationship between Mrs. Tigani and Bruce then further deteriorated.

In 2012, Bruce filed a petition to remove Mrs. Tigani as executrix of Mr. Tigani's estate and as trustee of Mr. Tigani's trust and requested an accounting of the administration of the estate and trust. Shortly thereafter, Mrs. Tigani amended her trust agreement again to remove Bruce and his children as beneficiaries. Mrs. Tigani then moved to dismiss Bruce's petition, arguing that he was only a contingent beneficiary that lacked standing. Bruce then challenged Mrs. Tigani's capacity to execute the 2011 and 2012 documents.

The Master issued a draft oral report recommending that the Court deny the motion to dismiss. Mrs. Tigani then further amended her estate documents. Specifically, she signed a codicil to her will in which she "irrevocably" exercised her power of appointment under Mr. Tigani's trust document and directed that the assets in the trust be distributed only to her two other children. The codicil further specified that no property subject to the power of appointment was to be distributed to Bruce. Finally, she directed that the codicil should be construed as a contract under seal to make a will between herself and her two other children in exchange for their continued love and affection and promise to assist with her care and maintenance for the rest of her life. The other two children signed an "acceptance" of the codicil in which they agreed to do the same.

Law: In Delaware, a "beneficiary" can bring an action to remove a trustee. The term "beneficiary" is undefined in the Delaware Code. Delaware law is silent as to whether a contract to exercise a power of appointment is enforceable, so the Master looked to the Restatement (which did not recognize such contracts) for guidance.

Holding: After a bench trial, the Master rejected Mrs. Tigani's position that Bruce was simply a contingent beneficiary. Rather, the Master ruled that Bruce, as a taker in default of a power of appointment, was a vested beneficiary subject to divestiture and was permitted under the Delaware Code to bring this petition.

The Master held that Bruce had standing to maintain his petition because Mrs. Tigani's testamentary power of appointment could not be exercised until her death. In other words, the 2012 codicil did not divest Bruce of standing because Mrs. Tigani's attempt to exercise the testamentary power of appointment was not effective during her lifetime. The Master explained that Mrs. Tigani must necessarily be deceased before any exercise of the power of appointment became effective. For that reason, any appointee that she designated could not claim an interest until her death.

The Master also held that the July 2012 codicil at most represented a release of her power to appoint but did not change Bruce's standing as taker in default of the power of appointment. The Master explained that a release of a power limits or eliminates the donee's power to appoint by reducing the class of permissible appointees of the power. However, even if the codicil was a release, Mrs. Tigani might elect not to exercise the power of appointment or fail to exercise it correctly, in which case Bruce would remain a beneficiary by default. Accordingly, the July 2012 codicil did not divest Bruce of standing.

Finally, the Master held that Delaware does not and should not recognize a "contract to recognize a power of appointment" as an enforceable agreement. The Master adopted the Restatement rule that such contracts are not enforceable with limited exceptions that were not applicable in this case. The Master recognized that enforcing such a contract in this case would run counter to Mr. Tigani's likely intent that Mrs. Tigani would have the freedom to exercise the power at any time prior to her death. In addition, the Master recognized that enforcing this agreement could confer a benefit on an impermissible appointee—in other words, if such a contract were recognized, Mrs. Tigani could confer a benefit on herself in exchange for the remainder interest that she had no right to enjoy herself under the trust agreement.

Practice Point: Because a testamentary power of appointment may only be exercised in a donee's last will and testament, Delaware courts will not enforce a contract to exercise the same during the donee's life. Accordingly, it is important that where a donee has a testamentary power of appointment, his or her testamentary documents that exercise that power should be frequently reviewed and, if necessary, amended so that the donee's present intent is accurately reflected in his or her estate planning documents.

This case is also significant in that it speaks to the status of a permissible appointee or taker in default of a power of appointment, and his or her rights under the trust. The comments to the Uniform Trust Code provide that the term "qualified beneficiaries" does not include appointees under the will of a living person, nor would it include the objects of an unexercised inter vivos power. *See* Unif. Tr. Code § 103(13), cmt. Some states expressly address such a provision; for example, Pennsylvania provides that qualified beneficiaries are determined "[a]ssuming nonexercise of all testamentary powers of

appointment." 20 Pa. C.S. § 7703. Trustees who are considering the rights of interested parties might consider whether to include takers in default of the exercise of powers of appointment and permissible appointees of a power of appointment.

Queen v. Schmidt, No. CV 10-2017 (PLF), 2015 WL 5175712 (D.D.C. Sept. 3, 2015)

Probate exception to federal jurisdiction does not apply where dispute involves a revocable trust, rather than a will

Facts: Ms. Douglass, resident of the District of Columbia, created a revocable trust agreement shortly before her death in 2010. Under the terms of the trust, Ms. Douglass appointed her estate planning attorney, Ms. Schmidt, as trust protector to monitor the administration of the trust by the designated trustees, with the power to remove the trustees.

After Ms. Douglass's death, the trustees and Ms. Schmidt had a disagreement over whether a certain parcel of real estate should be sold. When the trustees sold the property over the objection of Ms. Schmidt, Ms. Schmidt exercised her powers as trust protector, and she removed the trustees and appointed two independent accountants as successor trustees. The removed trustees sued Ms. Schmidt in the District of Columbia Superior Court for improper removal.

The complaint alleged that Ms. Douglass was vulnerable to persuasion at the time she executed the trust agreement and that Ms. Schmidt improperly drafted the trust agreement to name herself as trust protector in order to reap fees from the trust. Ms. Schmidt removed the case to the United States District Court for the District of Columbia. The Court's opinion addresses various procedural issues related to the removal and federal jurisdiction. In particular, the trustees argued that the probate exception to federal jurisdiction applied, such that Ms. Schmidt could not remove the action to federal court. The Court rejected this argument.

Law: Removal to federal court is permissible only when there is complete diversity among the parties. Under the so-called probate exception, federal jurisdiction is not appropriate for probate court matters related to the administration of a decedent's estate.

Holding: The Court ruled that complete diversity existed between the parties because Ms. Schmidt was a resident of Virginia, not the District of Columbia as plaintiffs had alleged. The Court held the probate exception did not apply because the matters at issue related to Ms. Douglass's revocable trust, not her estate. Accordingly, the Court held federal jurisdiction existed, and Ms. Schmidt could remove the action to federal court.

Additionally, the Court held the appointed successor trustees, although Florida residents, were subject to personal jurisdiction in the District of Columbia under (1) the District of Columbia's long-arm statute; and (2) Section 202 of the Uniform Trust Code, codified at Section 19-1302.02 of the District of Columbia Code. This DC Code provision states that a trustee submits to personal jurisdiction in the District of Columbia by accepting a trusteeship of a trust with its principal place of administration in the District of Columbia.

Practice Point: This case demonstrates that even when the underlying facts of a matter are a fairly straight-forward fiduciary dispute, federal court can still be a desirable option. Federal court might be particularly attractive to an out-of-state party or a national bank or trust company, whose counsel might

prefer the procedural rules of federal court. A party wishing to invoke federal jurisdiction must be careful to properly satisfy the jurisdictional requirements for filing in federal court.

Estate of Zucker, 122 A.3d 1112 (Pa. Super. Ct. 2015)

The exercise of a testamentary power of appointment in favor of certain descendants, to the exclusion of others, was proper under the terms of the trust instrument and the donee owed no duty of good faith to potential appointees.

Facts: Upon the death of Carl Zucker ("Carl") in 2002, his will created a marital trust for the benefit of his wife, Syma Zucker ("Syma"). Under the terms of the trust, Syma possessed a testamentary limited power of appointment exercisable in favor of any one or more of Carl's descendants. In her will, Syma exercised the power of appointment in favor of two trusts for the benefit of two of Carl's children, Scott and Karyn. This exercise excluded Wendy, a third child of Carl.

After Syma's death, Scott, as trustee of the marital trust, filed a petition for declaratory judgment in the Pennsylvania Orphan's Court, seeking a confirmation that Syma's exercise of the power of appointment was valid. Wendy objected to the exercise and claimed Syma's appointment was not a proper exercise of the power of appointment because it was made "in bad faith, based on hate and malice toward Wendy" and contrary to Carl's intention to treat his children equally. Wendy claimed Syma had a duty to exercise the power in good faith with fiduciary duties to the potential appointees. The Orphan's Court, on a motion for summary judgment, ruled that Syma's exercise of the power of appointment was valid. Wendy appealed.

Law: When exercising a power of appointment, a donee must exercise the power only within the scope of the authority granted by the instrument. When a power of appointment may be exercised to one or more persons to the exclusion of others, the donee may select among those persons as the donee determines.

Holding: On appeal, the Superior Court upheld the exercise of the power of appointment. Contrary to Wendy's assertions, the court held that a donee of a power of appointment is not a fiduciary and accordingly does not have fiduciary duties to potential appointees. Specifically, a donee does not have a duty of good faith, and may exercise the power for any reason the donee desires. The only limitation on the donee's exercise of the power is that it must be consistent with the terms of the governing instrument.

Practice Point: Powers of appointment are common estate planning tools often designed to provide flexibility to the estate plan and allow another person, such as a surviving spouse, to direct the disposition of trust assets in a manner appropriate under circumstances as they may develop and change over time. However, because the donee of the power may exercise the power in any manner consistent with the terms of the trust, and need not consider the desires of the settlor or the interests of the beneficiaries, settlors should carefully consider their intentions with respect to the breadth of the class of potential appointees.

Gladden v. Cumberland Trust and Investment Company, 2016 WL 1166341 (Tenn. Ct. App., Mar. 24, 2016)

Trustee cannot bind minor beneficiary to arbitration of future claims

Facts: The Alexis Breanna Gladden Irrevocable Trust was created after Alexis Gladden, a minor, suffered injuries that left her disabled. The trustee of the trust opened an investment account at Wunderlich Securities, Inc. ("Wunderlich"). The trustee signed an account opening agreement that required arbitration of any dispute between Wunderlich and the trust. In May 2012, Gladden's guardian sued Wunderlich and other defendants for breach of fiduciary duty, misappropriation of funds, and failure to properly manage trust funds. Wunderlich moved to compel arbitration, citing the account opening agreement. Gladden's guardian responded that the agreement was not enforceable. The guardian argued that the trustee lacked the authority to bind the trust to arbitration of future claims. The only language in the trust agreement concerning the trustee's power to agree to arbitration stated that the trustee may "settle, by compromise, arbitration or otherwise any and all claims or demands."

Law: In interpreting a trust document under Tennessee law, the grantor's intent is the primary consideration, and the court will first look to the four corners of the trust agreement to determine intent. The court will not consider parole evidence unless the trust agreement is ambiguous or there are allegations of fraud, mistake, or accident.

Holding: The court held that the trustee had the authority to agree to binding arbitration of claims once they had arisen. However, the court held that the trustee's power to "settle, by compromise, arbitration or otherwise any and all claims and demands" did not allow the trustee to submit to arbitration any claims that had not yet arisen. The court reasoned that to allow the trustee to agree to submit future claims to arbitration (1) would result in rewriting the agreement, which only allows the trustee to submit existing claims to arbitration, and (2) would be inconsistent with the trustee's duty to determine whether to arbitrate a claim based on the specific facts and circumstances of that claim. The court held that the trustee therefore lacked the authority to agree to arbitration of future claims when he opened the account at Wunderlich. As a result, the trustee's agreement to arbitrate claims against Wunderlich did not bind the trust.

Practice Point: This case follows a number of recent cases across the country, including *Monschke v. Timber Ridge Assisted Living, LLC*, 244 Cal.App.4th 583 (Jan. 29, 2016), discussed elsewhere in this Alert, that address the extent to which an arbitration agreement is binding on non-signatories. In another recent case, *Pinnacle Trust Co., L.L.C. v. McTaggart*, 152 So.3d 1123 (Miss. Dec. 4, 2014), discussed in a recent McGuireWoods Fiduciary Advisory Services alert, available here, https://www.mcguirewoods.com/Client-Resources/Alerts/2015/7/Recent-Fiduciary-Cases-July-2015.aspx, the Mississippi Supreme Court held that an arbitration provision contained within a wealth-management agreement between the trustee and trust advisor did not bind trust beneficiaries, at least under the circumstances of that case.

Financial institutions that manage trust assets typically require trustees to sign an account agreement, which might include language governing disputes between the financial institution and the trust. However, those agreements may not bind third parties, such as a beneficiary or, in this case, a beneficiary's guardian, unless the trustee has the authority to enter the agreement.

Financial institutions should consider whether a trustee has the authority to bind the trust to contract provisions, and, if it is determined under applicable law that the trustee may not have that authority, the financial institution might take additional steps to address that uncertainty. Additionally, attorneys who draft trust agreements should clearly address the powers the trustee does and does not hold. As this case law regarding arbitration develops, attorneys and other advisors can consider whether it is advisable to include a provision in a trust document that allows the trustee to submit future claims to arbitration.

United States v. Lazare, 2016 WL 1127627 (D. Nev. Mar. 4, 2016)

Federal court rescinds transfer as fraudulent, and enjoins future transfers from irrevocable trust, but finds trustee is not personally liable

Facts: Jon Edelman ("Edelman") was convicted of federal tax fraud in 1991, sentenced to five years in prison, and ordered to pay $334.8 million to the United States. Edelman escaped from federal prison in 1993, and, together with his wife and their three children, evaded capture for more than two years while they sailed the Pacific Ocean. He supported himself using funds from a trust he created before reporting to prison called the "Delos Trust." Edelman was caught in 1995 and re-imprisoned. Shortly after, his mother settled the Jon J. Edelman Trust (the "Edelman Trust") for the benefit of Edelman and his children. Edelman's mother funded the Edelman Trust with an income stream of $18,000 per month from her estate. Peter Lazare ("Lazare"), Edelman's longtime friend, became trustee of the Edelman Trust in 2004.

In 2012, the United States brought a tax collection action against Edelman, the Delos Trust, and the Edelman Trust. The United States also sought to enjoin Lazare from transferring assets from the Edelman Trust. While the injunction was pending, Edelman, Lazare, and a third person created the Aurora Borealis Trust, an irrevocable trust governed by Nevada law. Lazare then decanted the Edelman Trust's interest in the income stream to the Aurora Borealis Trust. After a trial, the court awarded the United States a constructive trust over the Edelman Trust in the amount of $1,601,000.

When the government attempted to collect against the Edelman Trust, it learned that Lazare had removed the trust's primary asset. Therefore, the United States brought this action against the trustees of the Aurora Borealis Trust and Lazare personally. The United States sought rescission of Lazare's transfer of the income stream from the Edelman Trust to the Aurora Borealis Trust under Nevada's fraudulent transfer laws. The government also sought to hold Lazare personally liable for the transfer under the Federal Priority Statute, 31 U.S.C. § 3713(b)

Law: Nevada's Uniform Fraudulent Transfers Act allows rescission of three types of fraudulent transfers: actual fraudulent transfers, constructive fraudulent transfers, and certain transfers by insolvent debtors. A transfer is fraudulent if it is made with the intent to hinder creditors or if the debtor does not receive "reasonably equivalent value" and knew or should have known that he would not be able to pay his debts as they became due.

The Federal Priority Statute, 31 U.S.C. § 3713(b), requires debtors whose liabilities exceed their assets and who have debts to the United States to pay the federal government before all other creditors. A personal representative of a debtor who pays another creditor before the federal government is personally liable for the payment amount.

Holding: The court held that the United States was entitled to rescission of the transfer of the income stream from the Edelman Trust to the Aurora Borealis Trust. The court found that the Edelman Trust received nothing in exchange for transferring the income stream to the Aurora Borealis Trust, the Edelman Trust was insolvent at the time of the transfer, and the United States' claim arose before the transfer was made. Therefore, the transfer was constructively fraudulent and a transfer by an insolvent debtor. The court rescinded the transfer and enjoined transfers from the Edelman Trust or the Aurora Borealis Trust to anyone other than the United States.

However, the court held that Lazare was not personally liable for the transfer of the income stream. The Federal Priority Statute applies to persons "indebted" to the United States, and the Ninth Circuit has held that a debt does not exist under the statute until the debtor's liability is certain. *See* 31 U.S.C. 3713(a)(1)(A). The court concluded that the Edelman Trust's liability to the United States was not certain when Lazare decanted the Edelman Trust, because the trust could have prevailed in the pending litigation. Therefore, Lazare was not personally liable for the transfer.

Practice Point: Irrevocable trusts are generally protected from the grantor's debts, and trusts with spendthrift provisions cannot be attached by the beneficiary's creditors. However, the law of fraudulent transfers may allow creditors to rescind an insolvent debtor's transfer to a trust, even if the creditors cannot recover against the trust. Furthermore, if the trust itself has debts to the federal government, the trustee must carefully follow the Federal Priority Statute. Trustees who wish to decant a trust to a second trust should also be mindful of the law of fraudulent transfers, as the decanting can be construed as a transfer of assets.

Berlinger v. Wells Fargo, N.A., 2016 WL 740521 (M.D. Fla., Feb. 25, 2016)

Facts: This opinion follows an earlier decision in this matter. *See Berlinger v. Wells Fargo, N.A.*, Case No. 2:11-cv-459-FtM-29CM, 2015 WL 6125529 (M.D. Fla. Oct. 16, 2015). This earlier decision was also the topic of a McGuireWoods LLP Fiduciary Advisory Services Alert, which is available here: [https://www.mcguirewoods.com/Client-Resources/Alerts/2016/2/ Recent-Fiduciary-Cases-February-2016.aspx](https://www.mcguirewoods.com/Client-Resources/Alerts/2016/2/Recent-Fiduciary-Cases-February-2016.aspx).

In this case, Rose Berlinger ("Rose"), her husband, and her mother each created trusts for the lifetime benefit of Rose's son Bruce and his descendants. Wells Fargo Bank, N.A. served as trustee of each of the trusts. Bruce's three children sued the trustee, alleging breaches of fiduciary duty related to the distribution and investment of trust assets. On a motion for summary judgment, the court concluded that the trustee had acted properly regarding the distributions from the trust for the benefit of Bruce, and the court further concluded that the trustee had the authority to invest trust assets in an interest in Bruce's residence given the broad investment discretion granted the trustee. However, given the dispute over the value of the property, the court did not grant summary judgment as to whether the investment was imprudent or made in bad faith.

At trial, the beneficiaries argued that the trustee violated the prudent investor rule when it paid $2 million for a one-third interest in Bruce's real estate. Each side presented a valuation in support of its position regarding the value of the real estate. The beneficiaries' estimate provided that the property was only worth $4 million total. The trustee countered that fair market value was $6 million, and therefore the trustee had paid fair market value for the interest in the real estate. The beneficiaries also demanded a jury trial under the Seventh Amendment.

Law: To prove breach of fiduciary duty under Florida law, a plaintiff must show: (1) the defendant had a fiduciary duty to the plaintiff; (2) the defendant breached that duty; and (3) damages to the plaintiff proximately resulted from the breach. The court found that breach of fiduciary duty and breach of trust are based on the same conduct, so it analyzed the claims together.

A plaintiff's right to a jury trial under the Seventh Amendment depends on balancing the factual issue to be tried and the relief sought. If the factual issue and the relief sought would have been "legal" questions in eighteenth century English common law, the plaintiff is entitled to a jury trial. A plaintiff is not entitled to a jury trial where the factual issue and relief sought would have been considered "equitable" questions. If the factors are split, the court will weigh the two to determine which factor is stronger.

Holding: The court held that the trustee had not breached its fiduciary duty by investing in real estate. The court rejected the estimate of the children's expert, finding that their expert was "not qualified" to appraise the real property, and the court found his methodology to be "simple but flawed." Instead, the court accepted the $6 million valuation from the trustee's expert. Applying this valuation, the trustee's purchase of a one-third interest in the property for $2 million did not breach the prudent investor rule.

The court also held that the beneficiaries were not entitled to a jury trial. Breach of fiduciary duty was considered a claim in equity in eighteenth century England. Additionally, the beneficiaries did not seek direct money damages, but rather an order compelling the trustee to pay the trust for the alleged breach. The court analogized this relief to restitution, an equitable remedy. Because the factual issue and relief sought were questions of equity, the beneficiaries were not entitled to a jury trial.

Trupp v. Naughton, No. 320843, 2015 Mich. App. LEXIS 1114 (Ct. App. May 26, 2015)

Court finds that the co-trustees triggered the termination provision of a trust through their actions

Facts: Elaine Trupp ("Elaine") created a trust in the late 1990's and designated three of her children—Brian, Donna and Deborah—as beneficiaries and co-trustees. The trust held a lakefront cottage and Elaine's residence in New Baltimore. The trust directed the children to make a schedule each year for the use of the cottage and to allocate the expenses of maintaining the cottage. The trust also allowed the trustees to terminate the trust and sell the cottage when they determined that continuing the trust was no longer justified. Lastly, upon Elaine's death, the trust transferred title to the New Baltimore residence to Brian, who in turn was to appraise the real estate and distribute to Donna its "fair market value" in cash.

After Elaine's death in 2008, the three children continued to use the lakefront cottage but did not agree on rules for the operation of the trust, such as scheduling use or dividing the cost of maintenance. For two years, Brian paid all of the bills without contribution from his sisters. Thereafter, he removed his personal property from the cottage and did not return. Deborah and Donna continued to use the property, and Deborah paid all of the bills.

Brian also took possession of the New Baltimore home after Elaine's death, but he did not obtain an appraisal of the real estate or distribute cash equal to its fair market value to Donna. In June 2010 he sold the property for $160,000. He did not pay Donna after the sale.

Brian petitioned the probate court to terminate the trust, sell the lakefront cottage, and require the other beneficiaries to reimburse him for their share of the expenses he had paid. The probate court granted Brian's request to terminate the trust, allowed the cottage to be sold, and required the beneficiaries to evenly divide the expenses—crediting Brian and Deborah for the amounts they had already expended.

The probate court also held that Brian was required to pay Donna, but it found that there was a latent ambiguity in the term "fair market value," as used in the trust. To resolve the ambiguity, the court relied on parol evidence to determine the amount owed. Specifically, the attorney who drafted the trust testified that Elaine intended that Brian would pay Donna the net value of the property after deducting the mortgage balance from the appraised value. The parties accepted the sale price of $160,000 in lieu of an appraisal, so the court deducted the mortgage balance and ordered Brian to pay Donna the $64,222.00 net value.

Donna and Deborah appealed both orders of the probate court, arguing that discontinuation of the trust was not justified when the court could have imposed rules by which the trust could continue to operate and that the court erred in considering extrinsic evidence to interpret "fair market value" because it is an unambiguous term.

Law: Michigan law provides that a trust may be terminated when the purposes of the trust have become impossible to achieve.

Additionally, in Michigan, when considering the meaning of a trust, the court must ascertain the settlor's intent from the trust document itself, unless there is an ambiguity. A patent ambiguity exists if the trust's meaning is facially uncertain, arising from the use of "defective, obscure, or insensible language" in the instrument. A latent ambiguity exists where the language and its meaning are clear, but some extrinsic fact creates the possibility of more than one meaning when the document's terms are executed.

Holding: On appeal, the court affirmed the orders of the probate court.

The appellate court found that terminating the trust was proper because the trust itself provided that the termination could occur when the trustees determine that discontinuation of the trust was justified. The actions of the co-trustees indicated such a determination. Though only one party explicitly sought termination of the trust, none attempted to fulfill the requirements of the trust. Moreover, the purpose of allowing the parties to share in the use of the cottage could not be met when none of the beneficiaries demonstrated an ability to follow the terms of the trust. Therefore, the probate court reasonably found that the purposes of the trust had become impossible to achieve.

The appellate court also held that extrinsic evidence may not only be used to clarify the meaning of a latent ambiguity but may also be used to demonstrate the existence of a latent ambiguity and to establish intent. The attorney responsible for Elaine's estate planning testified that Elaine had discussed her intent with him and wanted Brian and Donna to inherit the same net value. The court found that this intent could only be accomplished if the trust term "fair market value" was interpreted to mean net proceeds of the sale of the home. Thus, the probate court did not err in considering parole testimony to determine the trust's meaning of an otherwise clear term.

Practice Point: Actions of either the trustee or the beneficiary may make the purpose of the trust impossible and cause the trust to fail. Trustees must take care to implement the provisions of the trust, which may control both the distribution and the use of the property in trust.

Kelly v. Orr, 243 Cal. App. 4th 940 (Jan. 11, 2016)

Statute of limitations for professional negligence against an attorney for a trustee is tolled until the predecessor trustee's attorney-client relationship is terminated.

Facts: Beverly Clark executed her trust in 1999. She died in 2002, and her brother-in-law, George, served as trustee until he resigned in 2008. Though the trust designated Kelly as successor trustee, Beverly's daughter, Rebecca, seized control of the trust assets and succeeded George as trustee. Rebecca retained attorneys and acted on their legal advice throughout her time as trustee, paying their fees from the trust's assets.

On three occasions, Kelly and Wally (a beneficiary of the trust) tried to remove Rebecca as trustee. But on her attorneys' advice, Rebecca refused to resign. Eventually, on March 22, 2013, Rebecca agreed to resign, and Kelly replaced her as successor trustee.

On February 27, 2014, Kelly sued Rebecca's attorneys for professional negligence. He alleged that Rebecca's attorneys had negligently advised Rebecca in her capacity as trustee, causing over $300,000 of harm to the trust. The defendants demurred, arguing that Kelly's action for legal malpractice was barred by the one-year statute of limitations period.

The trial court sustained the defendants' demurrer, finding that Kelly knew of the defendants' alleged negligence no later than August 2012, more than one year before he filed suit. Though Rebecca did not resign as trustee until March 2013, Kelly was not precluded from suing the defendants before then and was not entitled to tolling because the defendants had not represented Kelly. Kelly appealed this judgment.

Law: California's continuous representation tolling provision applies to toll legal malpractice claims brought by successor trustees against attorneys who represented the predecessor trustee.

Holding: On appeal, the court reversed, holding that the statute of limitations was tolled until March 22, 2013—the date the defendants ceased representation of the predecessor trustee.

In California, legal malpractice claims are restricted by a one-year statute of limitations. However, that period is tolled during the time the attorney continues to represent the plaintiff regarding the specific subject matter in which the alleged wrong occurred.

The court found that when a fiduciary hires an attorney to advise in trust administration, the fiduciary, in his capacity as fiduciary, becomes the attorney's client. Moreover, a successor trustee acquires the same powers the predecessor had with respect to trust administration. This includes the power to commence a legal action for the benefit of the estate.

Thus, the court held that, as successor trustee, Kelly assumed Rebecca's right to toll the statute of limitations for the duration of the defendants' representation of Rebecca. It was immaterial that the defendants never represented Kelly because successor trustees stand in their predecessor's shoes with respect to legal malpractice claims against their predecessor's attorneys. The defendants continued to represent Rebecca as trustee on matters related to and intertwined with her service as trustee until March 22, 2013, when she resigned. Kelly's suit—filed less than one year after Rebecca's resignation—was therefore timely. The court held that the statute of limitations began to run when the predecessor trustee's attorney-client relationship ended and not when the successor discovered the alleged negligence.

Practice Point: In order to protect the interests of the estate they administer, trustees may sue their predecessor's attorneys for legal malpractice that has harmed the trust. The statute of limitations period will not begin to run until the predecessor ends the attorney-client relationship.

Estate of Gilliland, No. B262482, 2016 WL 109882 (Cal. Ct. App. Jan. 8, 2016)

Trustee's delay in distributing trust proceeds was not ruled a per se breach of fiduciary duty, even though trust value declined in the interim.

Facts: Elsinore Machris Gilliland created a trust in 1967, directing the trustee to pay $25,000 per year from the trust's income to each of her five nieces and nephews. Upon the death of the nieces and nephews, distribution would continue to their issue, until that "family line" (the life annuitants) ended. The balance of the annual net income was to be distributed to six named charities. These charities would also receive the residue of the trust estate upon termination of the trust. The trust document granted the trustee broad discretion in the exercise of its distribution power. Beginning in 2001, Union Bank of California N.A. ("Union Bank") served as the sole trustee.

In 2007, the life annuitants and the charities entered into a settlement agreement to modify the trust. All but $4 million of the trust corpus would be distributed to the charities, and they would in turn purchase commercial annuities for the life annuitants' benefit to increase their annual income. The agreement was conditioned upon the IRS issuing a private letter ruling that the commercial annuities' value would not be presently taxable to the life annuitants. The modification mandated that the trustee "shall distribute … upon receipt" of the favorable private letter ruling.

On September 24, 2008, the IRS delivered a favorable ruling to Union Bank. At this time, the trust's assets were worth approximately $72 million. On October 2, Union Bank's attorney requested instructions from the charities regarding whether they wanted the assets to be distributed in kind or in cash. Mr. Poindexter, an attorney who represented three of the charities, replied on October 29 and requested that Union Bank "hold up" distribution while the charities decided. By November 14, all of the charities had authorized distribution in cash. Union Bank proceeded to liquidate and distribute the trust's assets from November 19 through December 3; by then, the corpus's value had declined by over $11 million.

The charities petitioned the probate court to surcharge Union Bank as trustee for the loss of the trust's value. They argued that Union Bank breached its fiduciary duty by its delay in distributing the trust corpus after receiving the IRS letter. The probate court found the trustee had not committed a per se breach. It was proper to inquire as to how the charities wanted the assets to be distributed, and it was reasonable to heed the "hold up" letter from Mr. Poindexter, who had the leadership role among the charities' lawyers.

Two of the charities appealed, asserting that the probate court erred by not finding that the trustee committed a per se breach of fiduciary duty.

Holding: On appeal, the court affirmed the probate court's judgment.

The court noted that the trust modification required the trustee to distribute "upon receipt" of the favorable private letter ruling. It interpreted "upon receipt" as a triggering condition for when distribution would occur, but not how quickly the trustee should distribute. Looking to the Restatement Third of Trusts § 89, the court held that in California, delay may result in implementing a

plan for distribution of the trust. Trustees may exercise discretion to determine what is in the best interest of the beneficiaries and reasonable under the circumstances.

Therefore, the court held that Union Bank had not per se breached its fiduciary duty by asking the charities for authorization and instructions within eight days of the triggering condition. The Restatement and the trust itself gave the trustee discretion in making distributions, and Union Bank's attorney believed it was prudent to seek instructions. Union Bank likewise had not committed a per se breach of its fiduciary duty by waiting to proceed with distribution until November 19, 2008. The "hold up" letter reasonably indicated that not all of the charities had decided what kind of distribution they desired, and Union Bank received the last authorization only five days before it commenced the distribution process.

Practice Point: Trustees should ensure that they are exercising reasonable discretion in delaying the distribution of a trust corpus, and should document the reasons for any delay in the timeline of the distribution. If a court finds that the delay is unreasonable or an abuse of discretion, it may find that the trustee has breached its fiduciary duty and hold the trustee liable for a decline in the trust's value.

McDevitt v. Wellin, 2016 WL 199626 (D.S.C., Jan. 15, 2016)

Court holds that trustee and trust protector are not entitled to payment of fees or segregation of trust funds before final judgment.

Facts: Keith Wellin ("Wellin") created an irrevocable trust under South Dakota law for the benefit of his three children. In 2013, the children, as trustees of the trust, liquidated the trust's assets, including about $100 million in stock, and distributed the proceeds outright to themselves as the trust beneficiaries. The trust protector, Lester Schwartz ("Schwartz"), sued the children, alleging that they had tortiously and improperly terminated the trust. However, as discussed in an earlier McGuireWoods case summary, available here, https://www.mcguirewoods.com/Client-Resources/Alerts/2014/6/Recent-Cases-of-Interest-to-Fiduciaries.aspx, the Court found that Schwartz's status as trust protector did not impart standing to sue. Therefore, Schwartz appointed Larry McDevitt ("McDevitt") as an additional trustee, and McDevitt ratified Schwartz's action against the children.

Schwartz and McDevitt filed a motion to require the children to reimburse the trust for trustee fees, trust protector fees, and attorneys' fees incurred before and during the litigation. The motion also sought to segregate funds for future fees. Schwartz and McDevitt argued that segregation was necessary to prevent the children from spending trust assets that would be needed to cover the judgment Schwartz and McDevitt sought. The children countered that neither state law nor the trust agreement empowered Schwartz and McDevitt to seek reimbursement. Therefore, the children argued, the motion sought injunctive relief through the court's equity powers. Courts require litigants to satisfy a higher burden of proof when seeking equitable orders. The children argued that Schwartz and McDevitt could not satisfy the higher standard. Notably, Wellin advanced Schwartz and McDevitt's fees and the litigation costs, and Schwartz and McDevitt were required to reimburse Wellin only if they prevailed in the litigation.

Law: Injunctive relief includes all equitable orders that require a party to comply or face contempt charges. A court will issue a preliminary injunction only if the parties seeking the injunction show that: (1) they are likely to succeed on the merits of the claim; (2) they will suffer irreparable harm in the absence of the injunction; (3) the balance of the equities favors the injunction; and (4) the injunction is in the public interest.

Holding: The Court found that neither state law nor the trust agreement empowered the court to award Schwartz and McDevitt's fees before the final judgment. Therefore, the Court applied the four-factor test for injunctive relief. The Court rejected Schwartz and McDevitt's argument that the injunction was necessary to prevent the children from spending the trust assets that would be needed to pay their fees. Wellin had already advanced Schwartz and McDevitt's fees and the litigation costs, and Schwartz and McDevitt were not required to reimburse Wellin unless they prevailed in the litigation. The Court concluded that because Schwartz and McDevitt's fees and litigation costs would be paid regardless of the outcome of the claim, they could not show a risk of irreparable harm. Therefore, the Court denied the injunction.

Practice Point: Applicable state law might not provide statutory rights for trustees and other persons hired by the trust to segregate trust funds during litigation with the beneficiaries. Therefore, trustees should consider provisions in the trust agreement governing this issue. If not, the trustee may need to resort to the court's equitable powers, in which case the trustee will need to satisfy a more demanding burden of proof.

In re Estate of George Mathai (2014-482, NYLJ 1202716307504, at *1 (Surrogate's Court, Jan. 7, 2015)

Court addresses grounds for finding a potential administrator of an estate ineligible to administer the estate and evidentiary requirements and burdens of proof related thereto.

Facts: The decedent's children from a prior marriage objected to the petition of their stepmother, Saramma George ("Saramma"), for letters of administration. The children claimed that Saramma was unfit for appointment as a fiduciary, alleging that she was (i) dishonest, (ii) hostile towards them, and (iii) potentially improvident in handling the decedent's estate. The children further challenged the validity of Saramma's marriage to the decedent, alleged that the decedent left a will, and sought to compel its production. They also cross-petitioned for letters of administration to be issued to one of the children. Saramma moved for summary judgment, seeking to dismiss the children's claims as frivolous and meritless. The Court's opinion addresses the requirements and burdens of finding a person ineligible to receive letters of administration.

Law: Under New York law, a person may be found ineligible to receive letters of administration if he or she "does not possess the qualifications required of a fiduciary by reason of substance abuse, dishonesty, improvidence, want of understanding, or … is otherwise unfit for the execution of the office." The surviving spouse has a statutory priority to receive letters of administration. The burden of proving ineligibility lies with the person objecting to the qualification.

Holding: The Court granted the Petitioner's summary judgment motion seeking letters of administration. The Court ruled that the children did not meet the level of proof required to demonstrate that Saramma was dishonest or improvident. To prove dishonesty, an objectant must show a tendency or "habit of mind toward wrongful action", or "dishonesty in money matters from which a reasonable apprehension may be entertained that the funds of the estate would not be safe in the hands of the (fiduciary)." To show improvidence, the child must show actions that "would be likely to render the estate unsafe and liable to be lost or diminished" or misappropriation or mishandling of the decedent's property). The Court also rejected the children's claim that Saramma should be disqualified based on her hostility towards them, holding that only disharmony which "jeopardizes the interests of the beneficiaries and the proper administration of the estate" was grounds

for Saramma's disqualification. The Court dismissed the children's claims related to the validity of Saramma's marriage to the decedent and the existence of a will, concluding that these claims were without evidence and mere conjecture and speculation.

Practice Point: Courts will view carefully claims of beneficiaries or distributees seeking to impose their preference of fiduciary contrary to the testator's choice of fiduciary (or contrary to the statutory order of priority).

United States v. Read, 2016 WL 310721 (D. Conn 2016)

Trustee held liable for taxes after making distributions from trust while trust owed income tax.

Facts: In 1999, Randy Read established a trust worth over $700,000 for his children with stock options that his wife had earned and himself as trustee. In 2000, the trust filed a request for an extension of time to file its tax return; the request showed that the trust had a tax liability of $121,707.00. Read was aware of the tax liability in April of 2001. On April 30, 2001, the trust had assets worth $225,170.80. On June 29, 2001, the trust's value was $162,869.27.

Between July 5, 2001 and July 30, 2001, Read made four payments to carpenters totaling $25,000 for home renovations. On July 31, 2001, Read disbursed $25,000 from the trust fund to himself, bringing the trust's value to $108,390.02. IRS records revealed that the trust's tax liability was at least $121,749.00, which meant that Read's July 31, 2001 disbursement decreased the trust's value to a level below its tax liability, rendering the trust insolvent. From July 2001 to January 2010, although the trust's value never exceeded its tax liability, market gains and dividends allowed Read to disburse at least another $197,771.35, including the $25,000 disbursement on July 31, 2001.

Read spent some of the money to renovate his house, to invest in real estate, to pay for his children's private preschool education, and to send the children to summer camp. Read also wrote about $80,000 in checks directly to himself. The IRS sued Read individually and as trustee of the trust, contending that Read made payments from an insolvent trust that had an outstanding tax liability and moved for summary judgment, seeking $175,042.16 plus prejudgment interest.

Law: An insolvent person who is indebted to the United States must first pay the claims of the United States before voluntarily assigning property to others. Under 31 U.S.C. § 3713(b), a representative of an insolvent person or estate paying any part of a debt of the person or estate, or making a distribution therefrom, before paying a claim of the United States may be held personally liable to the extent of the payment for unpaid claims of the United States if he knew or had notice of facts that would lead a reasonably prudent person to inquire as to the existence of a debt owed to the United States.

Holding: The Court ruled that because Read: (1) was a trustee of the trust and was the only person with check-signing authority for the trust, (2) was aware of the tax liability, and (3) rendered the trust insolvent by his July 31, 2001 payment of $25,000 to himself, Read was personally liable for the entire amount of the debt owed by the trust. The Court also awarded prejudgment interest to the United States despite its recognition of the fact that most courts decline to make such an award.

The Court held that three factors weighed in favor of awarding prejudgment interest: (1) the need to fully compensate the wronged party for its damages weighs in favor of prejudgment interest, (2) considerations of fairness weigh in favor of awarding prejudgment interest because Read's self-dealing transfers of some of the trust's distributions enriched himself and his family at the public's expense,

and (3) the remedial purpose of the statute (to secure adequate revenue for the United States) weighs in favor of prejudgment interest.

Practice Point: This case demonstrates that trustees may be held personally liable for making distributions from an insolvent trust if they know or should have known of a debt owed to the United States. Furthermore, courts are not opposed to awarding prejudgment interest to the United States in cases where the trustee's post-insolvency payments benefit the trustee and/or the United States will not be made whole without payment of such interest.

Schrage v. Seberger Living Trust, 2016 WL 914796 (Ct. App. Ind., March 10, 2016)

> **When the beneficiary of a specific bequest under a trust agreement sought a complete, unredacted copy of the trust agreement from the trustee, the court held that income and remainder beneficiaries were entitled to receive complete copies of a trust agreement by statute but recipients of specific bequests were not.**

Facts: Audrey Seberger ("Audrey") created the Audrey R. Seberger Living Trust in 1992. During her lifetime, Audrey amended and restated the Trust several times, most recently in 2009. A 2009 amendment to the trust instrument disinherited Jill Schrage, the mother of the appellant, Stephanie Schrage ("Stephanie"). The 2009 amendment to the trust directed that Stephanie receive $25,000 at the death of Audrey. Audrey died in 2014, at which time Stephanie requested a copy of the trust instrument from the trustee. In response, the trustee provided Stephanie with an excerpt from the trust instrument which showed Stephanie was entitled to receive $25,000 from the trust. The trustee also provided Stephanie with a trust certification which provided evidence of the trust's existence and contact information for the trustee.

The trustee filed a petition for instruction, asking the court to determine whether a specific distributee was entitled to receive a complete copy of a trust agreement under Indiana law. Stephanie separately filed a petition requesting that the court order the trustee to deliver her a complete and unredacted copy of the trust instrument. The trial court denied Stephanie's request and ordered the trustee to not provide her with a complete, unredacted copy of the trust agreement. Stephanie appealed.

Holding: On appeal, the Court of Appeals of Indiana affirmed the decision of the trial court.

The appellate court applied the *de novo* standard of review as the issue before the court was one of statutory interpretation. The court noted that by statute, income beneficiaries and remainder beneficiaries are entitled to receive a complete copy of a trust instrument. Stephanie argued that she was a remainderman because the specific bequest she was entitled to receive under the trust agreement would come from trust principal. The trustee asserted the Stephanie was not a remainderman and that she was not entitled to trust principal. Instead, the trustee argued she was merely entitled to a cash distribution before any income or principal of the trust was distributed to the remaindermen.

The Court reviewed Indiana's statutory language. The applicable statute provided that remainder beneficiaries are persons "entitled to receive principal when an income interest ends … and in which principal is property that is held in trust for distribution to a remainder beneficiary when the trust terminates." The Court also observed that the state's trust certification statute clearly anticipated that a document, other than the trust instrument, could be provided to someone with an interest in the trust and that trust excerpts are appropriate in certain circumstances. Importantly, the Court accepted the

trustee's argument that specific distributees like Stephanie do not have an ongoing interest in the administration of the trust because the rights of specific distributees are not affected by the ongoing administration of the trust. Accordingly, in affirming the lower court's order, the Court found that Stephanie, as a specific distributee of the trust, was not a remainder beneficiary of the trust, that she was not entitled to receive trust principal because the specific bequests were not being made at the termination of the trust and, therefore, she was not entitled to receive a complete unredacted copy of the trust agreement.

Practice Point: The trustee's duty to inform and report to the trust's beneficiaries is a central duty of all trustees. Depending on the trust instrument, a trustee's ability to fully disclose a trust instrument to beneficiaries can range from fully discretionary to highly restricted. State law will fill in the gaps where disclosure of the trust instrument is not addressed in the document. This trustee took the measured action of petitioning the court for instructions on disclosure of the document. The Indiana courts reached the same conclusion on this issue that many practitioners and fiduciaries reach, namely that specific distributees are generally not entitled to a complete copy of the trust instrument.

DeJohn v. Wheeler, 2016 WL 270033 (Ct. App. Cal., Jan. 21, 2016)

Court finds that mother, as trustee of the trust, and family's accountant, in his limited role as independent trustee of the trust, had not breached fiduciary duties owed to the daughter as beneficiary

Facts: Margaret and James Narron created the Narron Family Trust in 1991 (the "Family Trust"). The Family Trust was funded with several parcels of real estate located in California. James died in 1996. Following his death, the Family Trust was divided into a Decedent's Trust and a Survivor's Trust. Upon Margaret's death, the assets of both the Decedent's Trust and the Survivor's Trust would be distributed to her two children, Stephen and the appellee, Lisa. Margaret was a co-trustee of the Decedent's Trust (the subject of the litigation). The family's accountant, David Wheeler ("Wheeler"), was also designated as the independent trustee of the Decedent's Trust. Wheeler's authority was limited to approving distributions of income and principal from the Decedent's Trust to Margaret. Wheeler signed the trust document as trustee, but later testified that he forgot that he had agreed to serve as the independent trustee.

Margaret, as trustee, made loans from the Survivor's Trust to her son Stephen to assist him with the purchase and construction of a home in Colorado. To enable Stephen to complete the project, and to protect her earlier investments, Margaret, as trustee, also loaned Stephen funds from the Decedent's Trust. The record showed that at one point the Decedent's Trust had $1 million, but by the time of trial, the Decedent's Trust only had an approximately $80,000 promissory note. Stephen testified that he owed his mother approximately $1.2 million. There was conflicting testimony as to what distributions from the Decedent's Trust, if any, Wheeler approved for Margaret's benefit.

Lisa sought to surcharge Margaret and Wheeler for breaches of fiduciary of duty. She sought recovery from her brother and sought to hold the accounting firms with which Wheeler was affiliated vicariously liable for Wheeler's actions. The trial court found for Lisa on all counts, holding Margaret, Wheeler, Stephen and the accounting firms liable to repay wrongful distributions from the Decedent's Trust in the total amount of nearly $1.7 million (including interest).

Holding: On appeal, the Court held that Margaret, Wheeler, and Wheeler's accounting firms were not liable to Lisa.

The primary issues on appeal were whether Margaret was authorized to repay distributions to the Decedent's Trust, whether Wheeler had approved distributions to Margaret from the trust, and whether the distributions made by Margaret were instead loans from the Decedent's Trust to Stephen. The appellate court found that Wheeler had approved monthly distributions to Margaret and held that such distributions were to be credited against Lisa's judgment as such distribution amounts were properly made from the trust. At trial, Wheeler also approved distributions of trust income to Margaret, and the appellate court permitted such retroactive approval. Thus, the Court held that Margaret was also entitled to credit for distributions of income she received from the Decedent's Trust.

On the loan issue, the court identified at least five documents in the record which, over many years, evidenced that Margaret was loaning funds to Stephen from the Decedent's Trust. Importantly, the Court also found there was no evidence that Margaret intended to make gifts of the funds distributed from the Decedent's Trust to Stephen. Moreover, Margaret was the sole trustee of the Decedent's Trust and she had the sole authority to manage the trust's property, including making loans of the trust property.

Wheeler's defense was aided by an amicus curiae brief filed by the California Society of Certified Public Accountants (the "Society"). Both Wheeler and the Society argued that Wheeler did not breach his duties under the Decedent's Trust because he had sole discretion to approve distributions to Margaret. Relying on the Third Restatement of Trusts, the Court effectively found that Wheeler was only a distribution trustee and that he could not be liable for the loans Margaret made to Stephen, because only Margaret had such authority. The Court found that Margaret had not sought Wheeler's approval of distributions (other than the previously recurring monthly distributions). The Court therefore concluded that Wheeler had not breached any duty under the Decedent's Trust and was not liable to Lisa for Margaret's distributions. The judgments against Wheeler's accounting firms were similarly reversed.

The Court also found that the successor independent trustee had standing to defend the action and affirmed one of the trial court's orders respecting Lisa's attorney's fees and remanded another. The Court then remanded the issue of whether the amount of prejudgment interest awarded to Lisa was reasonable for reconsideration in light of the Court's findings on the substantive issues in the case, which generally were very favorable to Margaret.

Monschke v. Timber Ridge Assisted Living, LLC, 244 Cal.App.4th 583 (Jan. 29, 2016)

> **Following decedent's death, arbitration clause signed by agent under decedent's power of attorney was not enforceable against personal representative of decedent's estate, at least in the case of a wrongful death action which was brought on behalf of the decedent's heirs, and not on behalf of the decedent's estate**

Facts: Starting in about 2005, Marjorie Fitzpatrick ("Marjorie") began suffering from dementia. In 2012, Valerie Monschke ("Valerie"), one of Marjorie's daughters, acting as agent under Marjorie's power of attorney, enrolled Marjorie in one of the facilities of Timber Ridge Assisted Living, LLC ("Timber Ridge"). Valerie, as Marjorie's agent, signed a residency agreement with Timber Ridge (the "Agreement"). The Agreement contained an arbitration clause, which provided in pertinent part that "all claims and disputes arising from or related to this Agreement or to your residency, care or services at Timber Ridge … shall be resolved by submission to neutral, binding arbitration." The arbitration

clause also provided that it was binding on "all parties to this Agreement and their spouse, heirs, representatives, executors, administrators, successors, and assigns, as applicable."

Marjorie died in October 2013. In April 2014, Valerie, acting as Marjorie's personal representative, filed a suit for wrongful death and elder abuse against Timber Ridge. Valerie alleged that Timber Ridge had failed to properly monitor Marjorie, allowing her to leave the facility and suffer injuries.

Timber Ridge moved to compel arbitration. The trial court denied the petition. The court concluded that California law provides that the wrongful death action was brought on behalf of Marjorie's children. And because the children were not parties to the arbitration agreement, the arbitration provision was therefore, not enforceable to require arbitration of the wrongful death action. The trial court also concluded that the elder abuse claim should be tried with the wrongful death claim, to avoid conflicting judgments. Timber Ridge appealed.

Law: The Court of Appeals summarized that in California, an arbitration agreement is only binding on a signatory, with certain exceptions, including that an agent under a power of attorney may bind the principal. The Court of Appeals concluded that in California, a personal representative who brings an action for wrongful death does so on behalf of the decedent's heirs, and not on behalf of the decedent or as the decedent's successor in interest.

Holding: The Court concluded that Valerie, as personal representative bringing an action for wrongful death on behalf of the children, was not deemed to be a signatory to the Agreement. Accordingly, the arbitration clause was not enforceable, and the wrongful death action could proceed to trial.

As to the issue of whether the elder abuse claim should be tried with the wrongful death claim, the Court of Appeals also confirmed the trial court's finding that submitting the elder abuse claim to arbitration could result in conflicting verdicts, and thus that the elder abuse claim should be tried with the wrongful death claim.

Practice Point: This case follows a number of recent cases across the country, including *Gladden v. Cumberland Trust and Investment Company*, 2016 WL 1166341 (Tenn. Ct. App., Mar. 24, 2016), discussed elsewhere in this Alert, that address the extent to which an arbitration agreement is binding on non-signatories. For example, in a 2014 decision, the California Court of Appeals concluded that when a beneficiary challenged the validity of a trust amendment that would insert an arbitration provision, the arbitration provision was not enforceable as to the beneficiary. *See McArthur v. McArthur*, 224 Cal.App.4th 651 (Cal. App. 1st Dist. 2014).

In *McArthur*, the Court reasoned that if the beneficiary had sued to enforce his or her rights under the trust agreement itself, then the beneficiary would be estopped from challenging the arbitration provision. In this case, the Court reasoned that if the personal representative brought an action on behalf of the estate, or as the decedent's successor in interest, then it would be more likely that the personal representative would be bound by the arbitration clause. This case can have important implications for parties who wish to enforce an arbitration agreement following a decedent's death.

In the Matter of Ronald J. Mount 2012 Irrevocable Dynasty Trust U/A/D Dec. 5, 2012, C.A. No. 10991–VCN, 2016 WL 297655 (Del. Ch. Jan. 21, 2016)

Delaware court denies motion to stay proceedings regarding Delaware trust pending the outcome of other litigation related to the settlor, the settlor's estate, and other trusts of the settlor, citing various factors

Facts: This lawsuit was part of a larger dispute among Ronald's son Ian Mount ("Ian"), Ronald's daughter Heather Mount ("Heather"), and Rene Giacalone Mount ("Rene"), Ronald's caretaker since 2007. Ronald purportedly married Rene in 2014, less than a year before his death. This larger dispute led to six actions, brought in Delaware, Florida, and New Jersey, and that generally, Ian argues that Heather and Rene acted together to unduly influence Ronald, to reduce Ian's interest in Ronald's estate and trusts.

Ronald established The Ronald J. Mount 2012 Irrevocable Dynasty Trust in 2012 (the "Trust"). The Trust recites that it is governed by Delaware law, and Wells Fargo Delaware Trust Company, N.A. is trustee. Under the Trust, Ronald was the lifetime beneficiary, and thereafter the beneficiaries were Ian and Heather. Kevin M. Kilcullen ("Kilcullen") was named as the Trust Protector. A distribution committee controlled distributions, and the committee was originally comprised of Rene and William Slattery (Ronald's long-time attorney). Kilcullen, as Trust Protector, had certain rights to remove and appoint members of the distribution committee. As to the Trust, Ian alleged that Heather and Rene acted together to have Kilcullen appointed as Trust Protector, and to appoint Rene and Heather as members of the distribution committee, so they could control distributions from the Trust.

Kilcullen brought this action to determine the validity of the Trust and to obtain instructions regarding its administration. Ian brought various counterclaims, including the removal of Kilcullen as Trust Protector. Ian moved to stay the action brought by Kilcullen in Delaware.

Law: When a Delaware court confronts the question of whether to stay an action in favor of another action, the court considers various factors, including the order in which the matters were filed, evidentiary issues, whether the dispute involves application of Delaware law, whether other similar actions are pending in another jurisdiction, and other practical considerations.

Holding: The Court denied Ian's motion for a stay, and allowed the action in Delaware to proceed. In so holding, the Court also concluded that the other actions did not directly involve the same issues brought by Kilcullen that related to the Trust, and therefore there was no significant risk of jurisdictional conflict.

Practice Point: The law regarding choice of law and the proper situs is complex; in addition, procedural issues can arise when actions concerning a trust or a beneficiary are brought in various jurisdictions. The case might have had a different outcome if the legal issues related to the Trust, and not only underlying factual issues regarding undue influence, were also pending in other jurisdictions. In a footnote, the Court also encouraged the parties to coordinate discovery, and the Court noted that it would become involved in coordinating that discovery, if necessary. In this case, the Court found that sufficient reasons did not exist to stay this proceeding in favor of other proceedings. Because a trust's choice of law and principal place of administration might allow the parties to bring an action in that jurisdiction, careful consideration should be given to the choice of law named in the instrument, and the place of administration of the trust.

Robert Rauschenberg Found. v. Grutman, No. 2D14-3794, 2016 WL 56456 (Fla. Dist. Ct. App. Jan. 6, 2016), *reh'g denied* (Feb. 24, 2016), *review denied*, No. SC16-502, 2016 WL 3185202 (Fla. June 8, 2016).

In a proceeding regarding a Florida trust, the trial court properly determined trustees' reasonable compensation based on various factors, and not based on a percentage of the trust assets or a lodestar method based on an hourly rate

Facts: The Robert Rauschenberg Foundation (the "Foundation") is the sole remainder beneficiary of the Robert Rauschenberg Trust (the "Trust"). The case stems from the administration of the very large estate of Robert Rauschenberg, whom the District Court of Appeal called an "iconic and prolific artist and philanthropist." The trustees had managed the Trust's assets for several years while its assets were transferred to the Foundation. During the trustees' administration of the Trust, the assets of the Trust increased from approximately $600 million to approximately $2.18 billion.

The Trust did not contain a provision providing for the trustees' compensation for their services. The trustees requested fees between $51 million and $55 million, based on factors set forth in *West Coast Hospital Ass'n v. Florida National Bank of Jacksonville*, 100 So.2d 807 (Fla. 1958). Quoting from *Bogert on Trusts & Trustees* § 976, the Court in *West Coast* concluded that these factors should include the following:

1) The amount of capital and income received and disbursed by the trustee;
2) the wages or salary customarily granted to agents or servants for performing like work in the community;
3) the success or failure of the administration of the trustee;
4) any unusual skill or experience which the trustee in question may have brought to his work;
5) the fidelity or disloyalty displayed by the trustee;
6) the amount of risk and responsibility assumed;
7) the time consumed in carrying out the trust;
8) the custom in the community as to allowances to trustees by settlors or courts and as to charges exacted by trust companies and banks;
9) the character of the work done in the course of administration, whether routine or involving skill and judgment;
10) any estimate which the trustee has given of the value of his own services; [and]
11) payments made by the cestuis to the trustee and intended to be applied toward his compensation.

The Foundation argued that the trustees were only entitled to $375,000 in fees, based on a lodestar method; that is, a reasonable number of hours at a reasonable hourly rate, which had been approved by Florida courts in cases of attorney's fees and for calculating the fees of a personal representative.

After hearing evidence of numerous factual witnesses and expert testimony, the trial court awarded the trustees $24.6 million in fees. Interestingly, while the trial court applied the 11 West Coast factors, the trial court's fee award of $24.6 million was approximately halfway between the request of the trustees ($51 to $55 million) and the request of the Foundation ($375,000). The Foundation appealed.

Law: Under Florida Stat. § 736.0708(1), a trustee is entitled to fees that are "reasonable under the circumstances," when the trust instrument does not specify a manner of calculating fees.

Holding: The court reasoned that, based on the legislative history of the Florida statute, the statute does not require the use of the lodestar method, and the statute instead requires the use of certain factors in considering the reasonableness of a trustee's fees. The Court of Appeal affirmed the trial court's calculation of the fee award, and specifically rejected the Foundation's position that the fee should be calculated based on the lodestar method.

Practice Point: The determination of trustee fees can be complicated, and can lead to further disputes regarding the reasonableness of those fees, particularly if the trust document does not specifically provide for a given trustee's fee. Because of this potential for litigation, trustees should review the structure of their fees before agreeing to serve in a fiduciary capacity, and should determine what records the trustee should retain in order to justify its fee if its fee is questioned.

Duckett v. Enomoto, No. CV-14-01771-PHX-NVW, 2016 WL 1554979 (D. Ariz. Apr. 18 2016).

> **Following a thorough and fact-specific inquiry of the terms of the trust, state law, and relevant case law, the Court held that an IRS notice of levy attaches to the beneficiary's interest in the trust despite the trustee's discretion to make distributions, although the Court found that there was insufficient evidence to determine whether the trustee should pay over the funds to the IRS pursuant to the Notice of Levy.**

Facts: Miyoko Enomoto ("Miyoko") died in February 2013. Nancy Duckett ("Duckett"), one of Miyoko's children, qualified as personal representative of Miyoko's estate. According to her will, $173,545 was held for the benefit of her son, Dr. Dennis Enomoto ("Dennis"), in a trust (the "Trust"). The Trust provided that the trustee "shall pay to [Dennis] so much or all of the net income and principal of the trust as in the sole discretion of the trustee may be required for support in the beneficiary's accustomed manner of living."

According to the IRS, Dennis failed to meet his tax obligations for tax years 2007 through 2011, and owed $701,079.11 to the IRS. In 2014, following Miyoko's death, the IRS served a Notice of Levy on Duckett. Duckett informed Dennis of the Notice of Levy, and when Dennis objected to paying the IRS any funds from the Trust, Duckett filed an interpleader in state court, and named Dennis, the IRS, and the trustee as parties. The IRS removed the action to federal court, then filed a motion for summary judgment.

The Court sought to determine the extent to which the levy attached to Dennis' interest in the Trust, and the extent to which the levy required assets from the Trust to be paid to the IRS. According to the Court, the two parties advanced "simpler, more practicable positions: the IRS says it is entitled to all the trust funds, and [Dennis] says it is not entitled to any."

Law: While state law might provide certain protections to property in a trust against the claims of a beneficiary's creditor—either because the trust is a "spendthrift" trust, or because the trust is a "discretionary" trust—those protections are not necessarily available to a beneficiary defending against federal tax claims asserted by the federal government.

Under 26 U.S.C. § 6321, the federal government may impose a lien on any "property" or "rights to property" belonging to a taxpayer. The United States Supreme Court has held that this language "is broad and reveals on its face that Congress meant to reach every interest in property that a taxpayer

may have." *See United States v. Nat'l Bank of Commerce*, 472 U.S. 713, 719–20 (1985). The determination of whether an interest in a trust is subject to levy is based on a two-part inquiry. First, the court must determine the taxpayer's rights to the trust under state law; then, second, the court must determine under federal law whether those rights amount to "property" or "rights to property" that are subject to the levy.

Application: The Court engaged in a helpful survey and summary of current law regarding "support" and "discretionary" trusts, and the application of federal tax liens to those trusts.

The Court noted that state law distinguishes between a "traditional support trust," in which the trustee must pay amounts to the beneficiary under an ascertainable standard, and a "traditional discretionary trust," in which the trustee has full discretion to make payments to the beneficiary, subject only to review for a trustee's abuse of discretion.

The Court concluded that in this case, the Trust contained elements of both, because the Trust provided that the trustee "shall pay" assets for Dennis' "support," and because the Trust also provided that those distributions would be made "in the sole discretion of" the trustee. The court concluded that the Trust was a "discretionary support" trust or a "hybrid" trust, and thus Dennis had a right to demand payments for his support, so long as the withholding of those payments "would constitute an abuse of discretion in applying an ascertainable standard."

The Court then engaged in a helpful summary of case law across the country which addressed whether a beneficiary's interest in a trust is subject to a federal tax levy. The Court concluded that this determination is "ad hoc," and based on the unique language of the trust and other circumstances.

Holding: The Court concluded that the Notice of Levy does "attach" to Dennis' interest in the Trust. However, the Court concluded that there was insufficient evidence to conclude whether the entirety of the Trust assets should be paid over to the IRS. The Court summarized, "the IRS has a valid lien but has not resolved the practical problems of enforcement."

Practice Point: In many states, a "spendthrift" or "discretionary" trust might automatically prevent a creditor of a beneficiary from attaching that beneficiary's interest in the trust or requiring distributions to the creditor. As this case illustrates, the question of whether a federal tax lien attaches to a beneficiary's interest in a trust proceeds under a different analysis. This analysis depends on the particular circumstances, including the particular language used by the settlor. A trustee who is served with a federal tax levy should proceed deliberately, to determine the extent to which the levy attaches to the beneficiary's interest, and the appropriate next steps in response to the levy. In some cases, it might be appropriate for a fiduciary to seek the guidance of the court, to determine the extent to which it must pay over any assets to the IRS.