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FIDUCIARY LITIGATION: SPOTLIGHTING INDUSTRY TRENDS

Chris Holtzclaw
Argent Trust Company
Ruston, Louisiana

Tuesday, May 2, 2023

10:30 AM – 11:30 AM
11:45 AM – 12:45 PM

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Mr. Holtzclaw serves as the Chief Fiduciary Officer for the Western Region of Argent Trust Company. The Western Region of Argent Trust Company includes all markets in Arkansas, Louisiana, Oklahoma, and Texas. Mr. Holtzclaw is responsible for all aspects of the personal trust and wealth management business of Argent Trust Company's Western Region including account administration oversight, business development, and risk and litigation management. In this role, Mr. Holtzclaw works closely with wealth advisors, trust officers, and investment officers to enhance the client experience and mitigate risks to the firm.

Prior to serving in his role as Chief Fiduciary Officer for the Western Region, Mr. Holtzclaw served as Corporate Counsel for Argent Trust Company's parent corporation, Argent Financial Group, Inc.

Mr. Holtzclaw earned a J.D. from Mississippi College School of Law and a B.S. in Economics from Louisiana Tech University. He currently resides in Ruston, Louisiana with his wife and four children. In his personal time, Mr. Holtzclaw enjoys coaching youth sports, fishing, and following state and local politics.

FIDUCIARY LITIGATION: SPOTLIGHTING INDUSTRY TRENDS
(2023 Edition)

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CASES OF INTEREST

I. DUTY TO INFORM AND REPORT

(A) *Kilian v. TCF Nat'l Bank*, 2022 Mich. App. LEXIS 6362 (Decided Oct. 20, 2022)

Background: Plaintiffs, David Kilian ("David"), individually and in his capacity as a Trustee of the Beryl Kilian Trust (the "Trust"), John Kilian ("John"), and Janice McKee ("Janice") are the children of Beryl M. Kilian ("Beryl") and the beneficiaries of the Trust. After Beryl's death in 1996, David and Empire National Bank served as Co-Trustees of the Trust. Seventy percent of the Trust's assets were set aside in a separate trust for the benefit of David, who struggled with mental health issues, and the remainder of the Trust was split between John and Janice. David was entitled to installments of income and property from the Trust. David also held a 5x5 power over the Trust assets. The Trust owned a majority share of Three Pines Resort (the "Resort"), and John and Janice owned smaller shares.

In 2000, David removed Empire National Bank as Co-Trustee and appointed as Co-Trustee defendant TCF's predecessor, Northwestern Bank, which was later acquired by Chemical Bank. Accounts were opened at Northwestern to manage the Trust and Resort. Statements for "B. Kilian Trust FBO David Kilian" from January 1, 2001 to March 31, 2014 reflected the beginning market value, receipts, disbursements, gains and losses, and an ending market value for the account and lists in detail each transaction. In the "portfolio assets detail" of the account statements, the Trust's miscellaneous assets were broken down into each parcel of property, with listed market values. For that account, the market value of $1,760,000 was broken down into $488,110 "Tax Cost Basis" and $1,271,890 "Unrealized G/L." Defendant issued similar statements for the "Kilian, Beryl Real Estate Trust Agency" account. Beginning on November 1, 2013, all of the account statements included language that, *"under MCL 700.7905(1)(a), a trust beneficiary has one (1) year from the date this report is sent to commence a proceeding claiming breach of trust ...."*

Between September 28, 2002, and October 3, 2016, David exercised his right to withdraw 5% of the value of the Trust under the 5x5 power. Beginning on January 6, 2011, David inconsistently began indicating what amount he was withdrawing. For instance, David indicated that he withdrew $50,000 on January 16, 2011, and $59,567 on October 15, 2012, but did not indicate what value he withdrew on October 17, 2011. In October 2014, David indicated that his withdrawal was calculated from the $1,274,112.91 fair market value of the Trust's financial assets, of which he stated that 5% was $63,706.15. In October 2015 he requested $57,223.77 without stating the basis for the amount. In October 2016, he requested $60,322.95, again stating that the amount was computed from the Trust's financial assets excluding real estate. *Each withdrawal was reflected in the account statements.*

Contact notes entered by Bank's agent between 2013 and 2017 reflect concern by the property manager about a person whom David had allowed to live in a cottage without a lease, as well as repeated indications that the property needed repair. The contact notes also reflect persistent overspending by David, struggles with mental health, and meetings in which David was informed that there was not enough money in the accounts to cover care and maintenance expenses for the resort. In 2016, the contact notes reflect the agent's belief that David was a challenging customer because of frequent overdrafts. The notes also indicated that, in 2017, David sold two of his vehicles to a maintenance person in lieu of payment. The Bank resigned as Co-Trustee on October 13, 2017, and in November 2017, $488,110 was distributed from the Trust's account.

In November 2019, Plaintiffs brought this action for breach of trust, waste, breach of fiduciary duty, and fraudulent misrepresentation, claiming that, among other things, Defendant had failed to keep adequate records of the Trust's expenses and operations, failed to keep the beneficiaries reasonably informed of the material facts necessary to protect their interests, and mismanaged the Resort. Plaintiffs alleged that the appraised value of the Trust's real estate assets remained unchanged despite customary practices to certify appraisals on a regular basis. Plaintiffs also alleged that Defendant failed to keep adequate records of expenses and operations and to keep the beneficiaries reasonably informed of the material facts necessary to protect their interests. According to Plaintiffs, they had no reason to expect that the financial information they received was incomplete or that the valuations were outdated or inflated. The plaintiffs also asserted that, because some of the resort's maintenance was funded solely by David, whose contributions were not reported in the agency accounts, the true financial condition of the resort had been concealed from them.

Defendant moved for summary disposition, arguing in pertinent part that the statute of limitations barred Plaintiffs' claims. Defendant asserted that, beginning in 2014, the monthly account statements informed Plaintiffs that if they believed that any duties had been breached, they had one year to commence proceedings for breach of trust. However, Plaintiffs did not file their complaint until November 4, 2019, more than a year after the Bank's final statement, despite that the previous financial statements had adequately disclosed the bases of Plaintiffs' claims.

Concerning plaintiffs' claims arising from events that occurred before April 1, 2010, the court granted summary disposition for Defendant on the basis that a provision in the Trust documents required a beneficiary to object to an accounting within 90 days from the receipt of the accounting. Concerning Plaintiffs' claims arising from events that occurred on or after April 1, 2010-the date that MCL 700.7905 took effect-the trial court granted summary disposition on the basis that the claims were barred by the one-year limitations period in MCL 700.7905(1)(a), which precludes a beneficiary from commencing a proceeding for breach of trust more than one year after the beneficiary or beneficiary's representative "was sent a report that adequately disclosed the existence of a potential claim for breach of trust and informed the trust beneficiary of the time allowed for commencing a proceeding." Plaintiffs appeal the trial court's ruling regarding the application of MCL 700.7905.

Holding: Affirmed. The Probate Court properly concluded that the Plaintiffs in this case were barred from bringing an action in November 2019 related to actions that Defendant took between April 2010 and November 2013, because Plaintiffs had received notice of the one year statute of limitations period in November 2013 report and should have inquired into the existence of their potential claims for breach of trust at this time.

Discussion:

(i) <u>Notice of Claims:</u> Plaintiffs unsuccessfully argued that, because the account statements before November 2013 did not include language that a beneficiary had one year to file a claim for breach of trust, Plaintiffs were permitted to bring claims related to conduct occurring before November 2013 for up to five years after Defendant resigned in October 2017.

The Court opined that Plaintiffs' interpretation would make different limitations periods apply depending upon whether a trustee included a notice in one report but not another, even if potential claims had been adequately disclosed in previous reports. This interpretation would not result in simplicity or clarity. The Court concluded that at the time of the November 2013 statement, the statements adequately disclosed the existence of potential claims for breach of trust before that date, plaintiffs had received "a report" that was consistent with MCL 700.7905(1)(a).

(ii) Adequacy of Disclosures: The Court concluded that the account statements adequately disclosed the potential breach of trust claims to the Plaintiffs. Plaintiffs' assertions that the account statements did not inform the beneficiaries and contingent beneficiaries of David's improper withdrawals, inaccurate real estate property values, and mismanagement of the Resort were all rejected by the Court. In no uncertain terms, the Court made it clear that the beneficiaries had sufficient information to know of a potential claim or inquire into the potential claim's existence.

(B) *Brock v. Brock*, 2022 Tenn. App. LEXIS 311 (Decided Aug. 10, 2022)

Background: J. Don Brock ("Decedent") died in March 2015, and his estate was distributed pursuant to his Last Will and Testament (the "Will"), which is the instrument creating the trust at issue. Decedent had executed the Will in October 2013. At the time of his death, Decedent was married to Sammye M. Brock, his surviving spouse ("Wife"). The Will established a marital trust ("the Trust") in order to provide income to Wife during her lifetime. The Trust provides that following Wife's death, the remaining assets of the Trust would be distributed between four beneficiaries, one of which is the Plaintiff-Appellant, Benjamin Brock ("Son"). Son is a 50% remainder beneficiary of the Trust, with three other individuals sharing an equal interest of the residual 50% remainder of the Trust. Wife and William B. Sansom (the "Trustees") were appointed as Trustees of the Trust.

In October 2019, counsel for Son sent a letter to the Trustees, which reflects that Son had received copies of the semiannual statements showing "the asset allocation for accounts of the Estate and Marital Trusts." In his letter, counsel for Son found these statements inadequate because they had not shown the distributions being made from the Trust or explained the changes in value of the assets. Son's counsel, therefore, requested further information regarding administration of the estate, including "more complete account statements showing increases and decreases in the value of the assets, the amount of any distributions from the accounts, and breakdown of whether the distributions are from income or principal," as well as identification of the source of income for the Trust and income tax returns for the estate and the Trust.

Counsel for the Trustees sent a responsive letter concerning Son's request in November 2019, explaining the contents of Decedent's Will and the Trust and informing him that he is not entitled to the information he had requested because he is a residuary beneficiary and not a current income beneficiary. Counsel stated that reports concerning the Trust's asset allocation had been voluntarily provided to Son by the Trustees but was not required under the terms of the Trust or the Tennessee Trust Code. The Trustees stated that as of the day of the letter, they intended to continue voluntarily providing the residuary beneficiaries of the Trust with semiannual reports but reserved the right to change that decision at any time.

The relevant provision in question reads as follows:

13.4 Reports. The fiduciary shall not be required to make any inventory or appraisal of the assets of my estate or any trust or to file reports, inventories or settlements with any court. However, the *fiduciary shall upon written request at reasonable intervals render to each then current income beneficiary of my estate or the trust estate, or to the natural or legal guardian of the beneficiary, full statements of all receipts and disbursements and a schedule of all assets and liabilities of the trust or my estate.*

In January 2020, counsel for the Trustees sent a letter to Son's counsel, informing him that they had withdrawn from representation. Following the withdrawal letter, counsel for Son sent a subsequent letter in February 2020 directly to the Trustees reiterating Son's request for information on the Trust and estate and requesting contact information for the Trustees' new counsel. Subsequently, newly-retained counsel for the Trustees sent a letter to Son's counsel in March 2020, incorporating and adopting the position stated in the previous November 2019 letter and reiterating that the Trustees had no reporting obligation to Son under the terms of the Trust and that Son possessed no authority to demand the information he was seeking to obtain.

In June 2020, counsel for Son sent a letter stating that the reporting section of the Trust did not expressly override the reporting requirements of Tenn. Code Ann. § 35-15-813 and simply stated that "no inventories, appraisals, reports or settlements are required to be filed in court." According to Son, the Trust expressly provides that those such reports must be made to the current income beneficiary but did not exclude the requirement in Tenn. Code Ann. § 35-15-813 that reports be made to all qualified beneficiaries upon request.

Subsequently, the Trustees filed a complaint for declaratory judgment, stating that a controversy had arisen and asking the Trial Court to "instruct them and declare whether the Trustees are required under the Trust and/or pursuant to Tenn. Code Ann. § 35-15-813 to provide the requested information about the financial affairs of the Trust to Son."

Son filed an answer to the complaint that included a counterclaim requesting the Trial Court to declare that the Trustees are required, pursuant to Tenn. Code Ann. § 35-15-813(a), to provide the requested information from the inception of the Trust to the present and going forward on at least an annual basis. Son further alleged a counterclaim of breach of trust on the part of the Trustees for refusing to provide Son with the requested information on the Trust. The Trustees filed an answer to Son's counterclaims, denying that they were required to provide Son with the information he requested or that they had breached their duty of trust.

The Trial Court subsequently entered an order in March 2021. In its order, the Trial Court recognized that Wife is the current income beneficiary of the Trust and that Son is a remainder beneficiary of the Trust, not a current income beneficiary. The Trial Court found that "on its face, the language used in Paragraph 13.4 of the Trust intended to ***override*** the reporting requirements of Tenn. Code Ann. § 35-15-813(a)(2)." According to the Trial Court, Decedent intended that the language at issue be "limiting" of the reporting requirements, rather than expanding the Trustees' reporting obligation to include additional duties for the current income beneficiaries. The Trial Court, therefore, granted Trustees' motion for judgment on the pleadings and denied Son's motion.

Holding: The Trial Court's Judgment is affirmed.

Discussion: The Tennessee Court of Appeals had to interpret Tennessee's adaption of UTC Section 813 specific to a trustee's duty to inform and report. Specifically, the Court had to determine if the Trust terms had overridden the reporting requirements in Tenn. Code Ann. § 35-15-813(a)(2) that the Trustee provide qualified beneficiaries with reasonable, requested information regarding trust activities when the reporting requirement was not expressly waived in the Trust.

The Court rejected Son's argument that Tenn. Code Ann. § 35-15-813(e) (Tennessee's "silent" trust statute) that requires statutory reporting requirements must be explicitly overridden by language in the trust instrument. The Court reasoned that is not what Tenn. Code Ann. § 35-15-813(e) requires and that Subsection (e) necessitates only that a written trust instrument "provide otherwise" in order to modify the statutory reporting requirements applicable to the trust. Clearly, Decedent provided otherwise in the Trust by limiting the Trustees' reporting obligation to only current income beneficiaries.

In a situation where the trustee's duty to inform and report is lessened in accordance with a trust instrument and governing law, written instructions provided by the settlor, trust advisor, or trust protector regarding this lessened duty to inform and report may be helpful. A written directive may serve as a nonjudicial substitute for instructions regarding interpretation of a trust and the settlor's intent.

II. QUALIFIED BENEFICIARIES

(A) *In the Matter of the Colecchia Family Trust*, 2021 Mass. App. LEXIS 219 (Decided Nov. 29, 2021)

Background: Michael Colecchia is one of six siblings whose parents were Mario and Lillian Colecchia. Mario and Lillian bought a house in 1955, where they raised their six children (Mario Jr., Michael, Mark, Denise, Donna, and Diane). On February 3, 2005, Mario and Lillian created an irrevocable trust (the "Trust") into which they transferred the property by quitclaim deed. Under the terms of the Trust,

"[t]he donors reserve the right to the use and occupancy of the real estate during their lifetimes, with the donors to pay for all maintenance and repairs, water and sewer charges, insurance charges, and taxes relating to said premises, if they shall so elect. At any time, the donors' right of use of the premises shall not include the right to collect rent therefrom. In addition, for further clarification, during the lifetimes of the donors, they shall have the right to possession or enjoyment of any real estate, which constitutes the principal residence. Nothing herein shall be construed to limit the ability of the Trustees to alienate, sell or convey the real estate or any interest therein, or to lease, mortgage or demise any or all the premises, so long as the provisions stated above are met."

According to the terms of the Trust, Mario and Lillian's children would receive nothing during Mario and Lillian's lifetimes. However, after Mario and Lillian both died, Michael and his brothers were each to receive ten percent of the Trust remainder. The remaining seventy percent was to be divided equally among the three daughters. Donna and Denise were named Trustees.

Michael did not know that his parents had transferred the property into the Trust. Nor did he know that his parents intended to distribute the trust assets unequally among their children. Believing that all six children would inherit equally, and that his parents (rather than the Trust) owned the property, from February 3, 2005 (the date on which Mario and Lillian created the trust and transferred the property to it) to February 2016 (when Lillian died), Michael maintained the property by landscaping the yard, removing snow from the sidewalks and driveway, renovating a bathroom, and performing general maintenance. Michael performed this work without compensation because he believed his parents continued to own the house and that all six children would inherit equally. Had he known otherwise, he would not have performed the work without compensation. After both parents died, Michael learned of the existence of the trust and of its terms.

Over Michael's objection, Donna and Denise, as Trustees, sold the property to a third party for $366,000 on January 1, 2017. The sale proceeds were held in the Interest on Lawyers' Trust (IOLTA) account of the attorney who represented the Trust in the transaction. Michael learned that the sales proceeds were deposited into an IOLTA for nine months, which he avers was both without right and unreasonably delayed distribution to the beneficiaries. Michael also contends that Donna and Denise failed to take reasonable steps to get the funds released from the IOLTA account, and in addition, that once the funds were released, Donna and Denise failed to place them in an appropriate interest-bearing account and delayed distribution to the beneficiaries.

Michael filed a general trust petition on May 23, 2018, attaching a complaint and a copy of the Trust. Count I of the complaint asserted that Denise and Donna breached their duty of loyalty by (1) not informing him that the Trust existed, (2) not informing him that Mario and Lillian no longer owned all interest in the property, (3) not dealing with Michael on fair contractual terms, and (4) accepting, and benefiting from, Michael's work on the property without disclosing the existence of the Trust or the fact that they would receive a greater share upon their parents' death. In count II, Michael alleged that the Trustees breached their duty of care by failing to put the proceeds from the sale of the property into an interest-bearing account and in failing to disburse the funds in a reasonable time. <u>Count III alleged that the Trustees had breached their duty to inform the beneficiaries of the trust and account for assets held by the Trust.</u> Count IV alleged that Denise and Donna took personal items from the property after Lillian died, and failed to make an inventory of those items or to disburse them properly. Count V asserted a claim of quantum meruit for the value of the work Michael performed on the property without compensation. Finally, count VI asserted that Donna exerted undue influence on Mario and Lillian, resulting in the unequal division of the property among their children.

For the purposes of this discussion, we will focus on Count III.

Holding: The Trial Court properly dismissed Count III alleging that the Trustees violated G. L. c. 203E, § 813 (*b*), by failing since the inception of the Trust to inform the petitioner beneficiary of the Trust's existence, where the Petitioner could not have become a qualified beneficiary until both of his parents had died, and his damages (i.e., that he would not have provided repairs, maintenance, and improvements to the property without compensation had he known of the Trust) were alleged to have occurred during his parents' lifetimes.

Discussion: The Court had to consider, among other matters, what is the point in time at which a person becomes a “qualified beneficiary” for purposes of a trustee's duty to inform under G. L. c. 203E, § 813. The Court concluded that, to determine whether a person is a “qualified beneficiary” for purposes of a trustee's duty to inform under § 813, the phrase “the date the beneficiary's qualification is determined” found in G. L. c. 203E, § 103, means the date, under the terms of the trust instrument, on which an event occurs to trigger a beneficiary's entitlement under the trust.

The Court further opined that the date triggering his entitlement to information as a qualified beneficiary began after Lilian’s death, because Michael could not become a beneficiary until both of his parents died.

III. VIOLATION OF MATERIAL TRUST PURPOSE

(A) *Skarsten-Dinerman v. Milton Skarsten Living Trust*, 2021 Minn. App. Unpub. LEXIS 996 (Decided Dec. 27, 2021)

Background: The Milton Skarsten Living Trust (the "Trust") was created in 2003 by Milton Skarsten ("Milton"), who passed away in 2017. The Trust named Milton's six adult children, including appellant Mary Skarsten-Dinerman, as its beneficiaries. The Trust further provided that the assets were to be divided into equal shares to create one share for each beneficiary.

The Trust assets originally consisted of four parcels of land. Milton, who was the original Trustee, sold some of the land before his death. The land now held by the Trust consisted of 507 acres of farmland. As of August 2020, the farmland was valued at $1,961,200, which reflects about a five-percent decrease in value from 2019 to 2020. The farmland lease was expected to produce a 2.7% annual rate of return in 2021.

The terms of the Trust provided specific instructions to the Trustee regarding the use and disposition of the assets, including the land, upon Milton's death. After specific expenses were to be paid from the Trust, the remaining balance of each share of the Trust was to "be retained in trust for the benefit of the beneficiaries" or their issue. Thereafter, the Trustee is to distribute equal shares of the Trust's net income to the beneficiaries or their issue "no less frequently than annually." The annual distributions continue until three of Milton's children pass away. Upon the death of the third of Milton's children, the Trustee is directed to distribute the remaining balance of each share of the Trust estate to the three surviving beneficiaries and by right of representation to the issue of any deceased beneficiary.

The terms of the Trust specifically addressed the potential sale of the land in two places. First, Paragraph IX of the Trust stated: "Except as expressly permitted by this paragraph, no sale of real estate included in the trust estate shall be permitted after my death." The referenced exception allowed for the sale of a portion of the land upon Milton's death, but only if the liquid assets of the Trust were insufficient to pay Milton's funeral expenses, estate taxes, and other specified debts. Second, Paragraph VII of the Trust gave one of Milton's daughters the right to occupy an existing residence located on one of the properties rent-free and prohibited selling that property without her consent. In addition to these specific references to real estate, the Trust also included a general provision in Paragraph VIII.E that requires the Trustee to exercise prudent judgment and care in "acquiring, investing, reinvesting, exchanging, retaining, selling, and managing" the Trust property.

In the summer of 2019, three of Milton's six children created special needs trusts for themselves, naming Skarsten-Dinerman as Trustee. Each of the adult children with special needs trusts assigned their beneficiary interests in the Trust to their respective special needs trusts.

Approximately one year later, Skarsten-Dinerman filed a petition to modify the Trust to allow the farmland held by the Trust to be sold and the proceeds distributed to the beneficiaries. The petition was brought pursuant to Minn. Stat. §§ 501C.0411(b), .0412(a) (2020), which allow courts to modify trusts under certain circumstances. Skarsten-Dinerman asked the court to modify the Trust for the following reasons: (1) the value of the farmland held by the Trust had decreased; (2) this decrease in value would result in reduced rent payments for the farmland and reduced income to the beneficiaries; and (3) the term of the Trust requiring distribution after the first three beneficiaries pass away would create an unequal outcome, because the first three beneficiaries to pass away would realize little benefit while the surviving beneficiaries would benefit substantially. The petition asserted that allowing for the sale of the Trust property before three of the beneficiaries passed away would not be inconsistent with Milton's intent or a material purpose of the Trust. _All beneficiaries consented to the Trust modification._ The petition also sought to recover costs, expenses, and attorney fees from the trust.

Skarsten-Dinerman later filed an amended petition asking the court to modify the trust to "permit and instruct the Trustee to *distribute* the real property assets" of the Trust to the six beneficiaries immediately (rather than waiting until the death of the third beneficiary), arguing that this distribution would not violate the prohibition on *selling* the real property assets in the Trust. The amended petition asserted that all beneficiaries supported the proposal.

The current Trustee, who was appointed in 2017, objected to the proposed modification on behalf of the Trust. He asserted that Milton's intent in creating the trust was to preserve the land for his children *and* ensure "that it would remain intact to provide a continuing source of income for them." The Trustee asserted that allowing the sale *or* distribution of the land would therefore directly contradict a material purpose of the trust.

The District Court denied Skarsten-Dinerman's petition to modify the Trust. It concluded that "the material purpose of the Trust was for all real property contained in the Trust to remain unsold, providing annual payments to the beneficiaries." Though the District Court found the Trust "ambiguous with respect to the sale of the real property assets," it ultimately concluded that Skarsten-Dinerman's proposed modification was inconsistent with Milton's intent and a material purpose of the Trust.

Skarsten-Dinerman appealed the District Court ruling.

Holding: The Appeals Court affirmed the decision of the Trial Court. The Appeals Court reasoned that the plain and unambiguous language of the Trust showed that Milton's intent and a material purpose of the Trust was to retain the farmland.

Discussion: Skarsten-Dinerman advanced two arguments: (1) modification is consistent with a material purpose of the Trust; and (2) modification is proper based on unanticipated changed circumstances not anticipated by the settlor.

The Appeals Court rejected both arguments. First, the Court opined that modification was inconsistent with a material purpose of the Trust because either the sale or the distribution of the Trust real property would conflict with a material purpose of the Trust. The Trust made it clear that the Settlor's intent was to retain the land as a source of income for the beneficiaries until three of the beneficiaries have passed away, even if selling or distributing the Trust assets would better serve the beneficiaries' current financial needs.

The Appeals Court further rejected the argument that unanticipated changed circumstances warranted modification of the Trust. To advance a changed circumstances modification, Skarsten-Dinerman should have proved that the modification would "further the purposes of the trust". The Court reasoned that the creation of special needs trusts for three of the beneficiaries and the decrease in value of farmland assets (and subsequent decreased rent) were not persuasive. In the end, the material purpose of the Trust was to retain the farmland as a source of continuous income for the benefit of the beneficiaries.

(B) *In re John O. Yates Trust*, 2022 Tex. App. LEXIS 9470 (Decided Dec. 28, 2022)

Background: On July 6, 1953, John O. Yates ("Yates") executed a will providing that his residuary estate be placed in Trust for his brothers and sisters and their issue per stirpes. The Trusts were to be administered as one. The Trusts were to continue until twenty-one years after the death of the last niece or nephew alive at the time of Yates's death, and the trust corpus would be distributed to the then-beneficiaries, the lineal descendants of Yates's siblings. The will also called for the creation of a trust advisory committee, consisting of designated family members, and instructed the trustee to consult with the advisory committee on important matters concerning the administration of the trusts.

After Yates's death on August 30, 1964, his will was admitted into probate and his residuary estate, which primarily consisted of various mineral interests and real property, was placed in the Trust. The residuary estate included the real property in Bexar County, which Yates referred to in his will as "my Bexar County home" and "my ranch home in Bexar County, Texas" (collectively referred to as the "Ranch"). Over the next five and a half decades, the real property and the mineral interests remained part of the Trust where principal and income were paid to the Trust beneficiaries.

On February 13, 2020, the Trustee, Frost Bank, San Antonio, filed an original petition seeking two declarations regarding the administration of the Trusts. First, the Trustee asked the Trial Court to determine if Yates's Trust authorized the sale of the Ranch in Bexar County. Second, the Trustee asked the Trial Court to determine if the Trust required the proceeds from the sale of the Bexar County Ranch to be allocated to the Trusts' principal account.

Robert Mack Yates, a Trust beneficiary, appeared in the suit and argued that the Trust's terms prohibited the sale of the Bexar County Ranch. Alternatively, Robert argued that even if the Trust authorized the sale of the Bexar County Ranch, it required the sale proceeds to be considered income rather than principal.

The Trial Court rendered a final judgment declaring: (1) the Trust authorizes the Trustee to sell the Bexar County Ranch, and (2) the sale proceeds from the Bexar County Ranch must be allocated to the Trusts' principal account. Robert appealed the Trial Court Judgment.

Holding: Affirmed.

Discussion:

(i) <u>Authority to Sell the Bexar County Ranch:</u> The language at the center of this issue appears in Article IX(m) of the Yates' Last Will and Testament:

I direct my Executor and Trustee to pay all taxes, insurance and normal repairs and other expenses in connection with the maintenance of my ranch home in Bexar County, Texas and my ranch in Duval County, but the cost of same shall be chargeable in equal proportions to such one or more of my brothers and sisters or nieces and nephews that shall desire to use the same. Otherwise, my Executor and/or <u>Trustee shall, with the consent and approval of the Advisory Committee,</u> ***<u>lease or otherwise dispose of</u>*** *<u>said properties</u> and the rentals or proceeds shall become part of the income or principal of the trusts created under my Will in equal parts or by stirpes as the case may be.*

Robert argued that Article IX(c) of the Last Will and Testament prohibits the sale of the Ranch. Article IX(c) stated that, "Except as otherwise may be provided herein, my Trustee . . . shall not have the authority to sell, convey or dispose of any of the trust property or any part thereof." The Appeals Court rejected this argument because Article IX(c) creates an exception to the general rule of prohibiting the disposal of Trust property.

In affirming the Trial Court's decision, the Appeals Court made it clear that term "dispose of" in Article IX(m) of the Last Will and Testament authorized the Trustee to sell the Ranch with the consent and approval of the Advisory Committee.

(ii) <u>Allocation of Sale Proceeds:</u> Robert argued that Article IX(m) of the Last Will and Testament clarified that receipts should be allocated to income was clear. The Appeals Court confirmed that the Trial Court correctly rejected this argument.

In affirming the Trial Court decision, the Appeals Court noted that the Last Will and Testament was clear that the Texas Trust Code would control. The Texas Trust Code provides that 'money or other property received from the sale . . . of a principal asset' 'shall' be allocated to the principal of the trust. Again, the Court referred to the plain language in Article IX(m) paragraph two specifically addressed the disposition of the Ranch. Article IX(m) paragraph two controlled over the general provision in paragraph one that all receipts are to be allocated to income.

This case has been appealed to the Texas Supreme Court.

IV. FIDUCIARY REMOVAL

(A) *In the Matter of the Leo Kahn Revocable Trust*, 2022 Mass. App. LEXIS 119 (Decided Dec. 12, 2022)

Background: Leo Kahn, a successful grocery store chain owner and early investor in Staples, created the Leo Kahn Revocable Living Trust (the "Trust") in 2006. Leo died in 2011. The Trust named Leo's wife, Emily, Joseph (Leo's son from a prior marriage) and Theodore Samet (independent) as Co-Trustees. Emily was a lifetime beneficiary of the two shares created under the Trust – the Spousal Trust and Family Trust. The Co-Trustees served alongside each other for nine years until Emily filed for removal of Joseph and Theodore in May of 2020.

Emily relied upon G.L.c. 203E, § 706(B)(4) of the Massachusetts Trust Code, which states:

"The court may remove a trustee if … removal is requested by all of the qualified beneficiaries, the court finds that removal of the trustee best serves the interests of all of the beneficiaries and is not inconsistent with a material purpose of the trust and a suitable co-trustee or successor trustee is available."

Joseph argued that the terms of the Trust prevent his removal. Specifically, Joseph first cited Article 16.06 which enumerated thirteen "for cause" grounds for removal. The first twelve items involve removal for trustee dishonesty and related actions of malfeasance, the thirteenth item included "any other reason for which a state court of competent jurisdiction would remove a trustee."

Second, Joseph pointed to Article 16.11, which applies <u>after</u> the death of Emily allowing for removal *with or without cause.* Joseph argued that the Articles, when read together, prevented his removal under § 706(b)(4) during Emily's lifetime.

Holding: Affirmed. The Court concluded that the Trust is ambiguous as to whether § 706(b)(4) can provide a basis for removing Joseph. The case was remanded to Probate Court for further proceedings.

Discussion: The Court weighed two central issues: (1) if the Trust is inconsistent with the MUTC, does the Trust provision prevail? and (2) if the Trust provision prevails, is no fault removal still permissible?

The Court opined that the terms of the Trust provision over any provision of the MUTC and cited the general rule set forth in Section 105(b) of the MUTC, which provides that "the terms of a trust shall prevail over any provision of the MUTC." The Court was clear that the trust provisions are construed as precluding removal under a basis such as § 706(b)(4).

The Court then addressed the second issue: whether the Trust precludes removal of a Co-Trustee pursuant to Section 706(b)(4). Applying a de novo standard of review, the Appeals Court found that the subject trust was ambiguous as to whether removal under § 706(b)(4) would constitute a 'for cause' or 'without cause' reason for removal. Considering this ambiguity, the Appeals Court found that the Probate Court erred in dismissing the action for removal under Section 706(b)(4) and that an evidentiary hearing to resolve this ambiguity was required in the Probate Court.

Application has been made the Supreme Court of Massachusetts.

V. ARBITRATION CLAUSES

(A) *Boyle v. Anderson*, 2022 Va. LEXIS 22 (Decided April 14, 2022)

Background: Strother Anderson created an inter vivos irrevocable trust that was to be divided in three equal shares to his daughter Sarah Boyle ("Boyle"), his son John, and the children of his son, Jerry. Upon Strother's death, Boyle became the Trustee and Beneficiary.

The Trust contained the following arbitration clause: "Any dispute that is not amicably resolved, by mediation or otherwise, shall be resolved by arbitration."

Linda, the widow of Strother's son, John, and the ancillary administrator of John's estate, filed a complaint against Boyle alleging that she had violated her fiduciary duties. Further, Linda sought to remove Boyle. Boyle filed a motion to compel arbitration. Linda opposed and asserted that the Trust was not a contract and that she, as a beneficiary, had not agreed to arbitration.

The Circuit Court denied the motion to compel arbitration. Boyle filed an interlocutory appeal asserting that the Circuit Court had erroneously ruled that the trust agreement could not qualify as a written contract or agreement under Virginia's Uniform Arbitration Act (VUAA) and the Federal Arbitration Act (FAA). The Virginia Supreme Court granted the appeal.

Holding: The Court of Appeals concluded that a trust is neither a contract nor an agreement that can be enforced against a beneficiary. Neither the VUAA or the FAA compel arbitration. The Circuit Court decision was affirmed and the matter was remanded for further proceedings.

Discussion: The Court of Appeals opined that a trust is, in general, a "donative instrument," not an "agreement between two or more persons which creates an obligation to do or not to do a particular thing." As such, a trust is not a "contract," as required to fall within the parameters of both the VUAA and the FAA. While the VUAA also compels arbitration for certain "written agreements," the Court rejected Boyle's argument that a trust qualifies as an "agreement." Further, the Court noted that an arbitration clause would not be enforceable under the VUAA as it relates to claims between a trustee and a beneficiary, as a beneficiary is not a party to any agreement. Along that same line, parties to contract are much different than that of a trustee and beneficiary in view of fiduciary duties owed.

Practitioners should review their state's law to determine if an arbitration provision in a trust is enforceable.

TOPICS OF INTEREST:

I. DIRECTED AND DELEGATED TRUSTS

Any trustee, in acting as a fiduciary, reviews their duties, obligations and responsibilities considering their risk, their time, and their reward (fee). Special consideration must be given before accepting a fiduciary role where duties are bifurcated among fiduciaries and non-fiduciaries.

Delegated trusts are generally existing trusts that do not contain bi-furcation language that allow for the separation of responsibilities. With a delegated trust, the trustee delegates certain responsibilities to a non-trustee. Most often, the trustee delegates the management of trust assets to an investment advisor. The conception of a delegation to an agent is not new to the trust landscape.

Alternatively, the concept of directed trusts are a recent phenomenon. Directed trusts are trusts in which certain of the powers traditionally vested exclusively in a trustee are instead divided among the trustee and other parties who may or may not be deemed to be fiduciaries, such as: (i) a trust protector with a broad range of directive powers; (ii) an investment advisor/trustee with exclusive power to direct investments; or (iii) a distribution advisor/trustee with the exclusive power to direct distributions.

Before accepting delegated or directed trust business, a trustee must consider the following:

i. Trust Code Considerations: Can the fiduciary role be properly bifurcated under governing law? If yes, is adequate protection afforded to your institution for acts of the co-fiduciary under the governing document or applicable law?

ii. Client Relationship: What firm is the point of contact for the settlor and/or beneficiaries? Establish appropriate lines of communication and boundaries with co-fiduciaries and the mutual client.

iii. Asset Custody: What firm will provide custody and safekeeping of client assets after examining distribution needs, accounting software reporting, and restrictions on withdrawals and transfers?

iv. Profitability: Is this profitable business for your firm given the added complexity and reduced fee for such fiduciary appointments?

v. Agreements with Co-Fiduciaries: Does your firm have a standard Delegation Agreement or Letter of Understanding to be executed by the co-fiduciaries?

vi. Internal Controls: Does your firm have established policies and procedures to take on this line of business?

An important consideration when vetting delegated and directed trust business is the concept of excluded fiduciary liability. In a directed trust, the trustee's role is limited to implementing the directives of the advisor or protector. As a result, the trustee may be excluded from certain decision-making responsibilities that are instead delegated to the advisor or protector.

However, if the advisor or protector makes a decision that results in harm to the trust or its beneficiaries, the excluded trustee may still be held liable for any resulting damages. To mitigate this risk, many directed trusts include provisions that limit the trustee's liability for decisions made by advisors or protectors. It is important to look to the governing instrument and applicable state law to determine if your firm is an excluded fiduciary.

The Uniform Directed Trust Act (UDTA) has been adopted in whole or in part in approximately 20 states. The UDTA includes provisions related to the liability of trustees, advisors, and protectors in a directed trust. Section 1004 of the UDTA provides that a trustee may be excluded from certain powers and duties if those powers and duties are granted to an advisor or protector. However, the trustee may still be held liable for any actions taken in bad faith or with reckless disregard for the trust's interests.

The UDTA also includes provisions related to the liability of advisors and protectors. Section 1012 of the UDTA provides that an advisor or protector may be held liable for any actions taken that are not in accordance with the terms of the trust or that result in harm to the trust or its beneficiaries. However, an advisor or protector may be exonerated from liability if the trust agreement specifically provides for exoneration and the advisor or protector acts in good faith and with reasonable care.

In conclusion, the acceptance of a delegated and directed trust will depend on a variety of factors, including the level of discretion desired by the settlor, the complexity of the trust's assets, and the potential for excluded fiduciary liability. Understanding the legal framework governing trusts, including the UTC and UDTA, can be helpful in making an informed decision regarding acceptance of prospective appointments.

II. FIDUCIARY INSURANCE

The fiduciary insurance marketplace has experienced adverse claim trends since 2019. This adverse trend is attributable to fiduciary liability insurance carriers defending the onslaught of excessive fee class action and employee stock ownership plan suits across the United States. The fiduciary insurance marketplace contracted as loss ratios from the largest fiduciary insurers skyrocketed. ERISA-related cases increased the frequency and severity of class action litigation against fiduciaries. The largest insurers who have remained in the fiduciary insurance business sharply increased premiums and deductibles, expanded underwriting, and required fiduciaries to “layer” limits with multiple carriers.

According to the Insurance Marketplace Realities 2023 – Fiduciary Liability Survey Report published by Willis Towers Watson (WTW), underwriters remain wary of fiduciary risks while insurers are more focused on retentions than on premiums. Increased retentions in the seven figure range remain commonplace for specific exposures, e.g., employee stock ownership plans, prohibited transaction, and excess fee exposures. Further, many insurers require layering of limits of insurance with multiple carriers with $5 million primary limits.

Although the marketplace is tumultuous, WTW predicts that flat renewals may become more commonplace given the previously limited market for primary fiduciary coverage shows signs of expansion.

It is important for your firm to review its policies of insurance on a frequent basis and work closely with a qualified agent well ahead of renewal periods.

III. CYBERFRAUD

According to the FBI's most recent Internet Crime Report, cybercrime continues to be a significant threat to individuals, businesses, and government organizations, with reported losses totaling over $10.3 billion in 2022.

The most prevalent cyberfraud in the United States is phishing, which involves the use of fraudulent emails, websites, or phone calls to steal personal information or money. Over 300,000 complaints were logged in 2022 with the average loss valued at approximately $126k!

Business email compromised (BEC) attacks account for over $2.7 billion in losses for 2022. BEC, which involves the use of email to trick individuals or organizations into transferring funds or providing sensitive information to cybercriminals posing as trusted entities, is a risk for institutions relying so heavily on client engagement through email.

To address the growing threat of cyberfraud in the United States, the FBI recommends that individuals and organizations take proactive measures to protect themselves. This includes regularly updating software and operating systems, using strong passwords, and being cautious when clicking on links or opening attachments in emails.

Additionally, the FBI recommends that individuals and organizations report any suspected cybercrime to law enforcement immediately, as this can help to identify and track down cybercriminals and prevent further losses.

In conclusion, cyberfraud continues to be a significant problem in the United States, with cybercriminals using increasingly sophisticated techniques to carry out their illegal activities. It is important for individuals and organizations to take proactive measures to protect themselves and report any suspected cybercrime to law enforcement. It is important that employees of your organizations to be trained to spot all forms of cyberfraud. Further, it is important to review and understand relevant policies of insurance that may cover a cyberfraud incident within your organization.

<u>Case to Watch:</u> *Disberry v. Employee Relations Committee of Colgate-Palmolive Company*, 2022 WL 17807188 (S.D.N.Y. December 19, 2022). While many cases involving theft of retirement plans have been filed against plan sponsors, recordkeepers and their custodians, none have resulted in clearly defining the responsibilities of fiduciaries. The *Disberry* case may provide needed clarity.

Paula Disberry worked for Colgate-Palmolive for a number of years. During that time, she contributed to the workplace Employee Savings and Retirement Plan and amassed a balance of approximately $750,000.00. Post-retirement, Disberry moved to South Africa and updated her contact information with the Plan (physical mailing address, email address, and cell phone number).

Disberry discovered that cybercriminals contacted the Plan through a telephone customer service center operated by Alight Solutions, the Plan's TPA. The cybercriminal updated her contact information and sent a temporary PIN by physical mail to Disberry's South Africa address of record with the Plan. It is alleged that the mail was intercepted and the PIN stolen. In February of 2020, the cybercriminals created a new permanent PIN and changed all account contact information.

Soon after, the cybercriminals requested withdrawals form the Plan account. BNY Melon, the Plan's Trustee, mailed a check for approximately $600,000.00 to the updated mailing address. The check was subsequently deposited in March of 2020. Disberry discovered the missing funds in September of 2020.

Disberry sued the Plan Committee, Alight Solutions, and BNY Melon for breach of fiduciary duty and maintained that the Defendants should have become suspicious of the fraudulent activity because:

(i) All of Disberry's contact information was changed and a subsequent distribution of the account balance was requested;
(ii) Disberry was not 59.5 years old, yet requested a full distribution;
(iii) The number of attempts to access Disberry's Plan account by both online and telephone access;
(iv) The cybercriminals attempted to access other Plans with different firms and were denied due to enhanced security protocols;
(v) The cybercriminals failed to contact the International Benefits Department despite this being a recommendation of the Plan prior to distribution; and
(vi) Disberry's information was split between two countries.

In response, Alight and BNY Melon denied they were fiduciaries. The Court agreed with this argument with respect to BNY Melon. The Court allowed the claims against Alight and the Plan Committee to proceed. The Court squarely rejected Alight's argument that they were not a fiduciary performing only ministerial duties; however, the Court explained that the denial of Alight's motion did not mean that Alight would ultimately be defined as a fiduciary.

Specific to the claim against the Plan Committee that survived a motion to dismiss, the Court stated that, "ERISA's 'fiduciary duty of care ... requires prudence, not prescience," and that "this is a very thin complaint as against the Committee. The case involves a fraudster executing on a complex, international scam. The Plan was a victim of fraud and theft just as much as the Plaintiff was. An ERISA plan is not required to have procedures in place that account for every possibility—i.e., to act as an insurer against all losses. It must adopt reasonable procedures, but not absolutely air-tight procedures, to protect against the possibility of what happened here, which was a heinous crime."

With little guidance for fiduciaries on steps to take to safeguard assets from cybercriminals, the outcome of this case will be closely watched by fiduciaries.

IV. ELDER ABUSE

According to the 2021 Council on Aging Report (the "Report"), financial exploitation of the elderly and vulnerable adults continues to grow in the United States. The Report found that financial exploitation is one of the most common forms of elder abuse, affecting approximately one in ten older adults in the United States. With 10,000 Baby Boomers turning 65 years old every day, financial exploitation of elderly and vulnerable adults will continue to increase. Financial firms must remain well-trained and vigilant to protect this class of customers.

Financial exploitation can take many forms, including identity theft, investment scams, and misuse of funds or property. The Report found that the most common form of financial exploitation is financial abuse by a family member, accounting for nearly 60% of reported cases. Further, the Report found that theft equated to approximately 28% of the abused adult's net worth (exclusive of home equity). Caregiver financial abuse is also a significant concern, with nearly 20% of reported cases involving a caregiver taking advantage of their position to exploit an elderly or vulnerable adult.

In addition to the impact on the individual's overall health and well-being, financial exploitation also has significant economic implications, with estimated costs of financial abuse of older Americans reaching $36.5 billion annually.

It is imperative that financial firms implement policies and procedures to address the exploitation of elderly and vulnerable adults. To protect elderly and vulnerable adult clients, consider implementing a trusted contact authorization form that allows the financial institution to speak with a trust contact in the event that exploitation is suspected.

Additional resources concerning elder abuse may be found by visiting the Department of Justice website at www.justice.gov/elderjustice/find-support-elder-abuse or the National Adult Protective Services website at www.napsa-now.org/help-in-your-area/.

The Future:

The Financial Exploitation Prevention Act (the "Act"), a bipartisan bill recently passed in the U.S. House of Representatives, will provide additional protections to both seniors and financial institutions if passed into law. This legislation would codify an existing FINRA Rule and Securities and Exchange Commission guidance that allows for certain firms to delay redemptions of securities if the exploitation of an elderly or vulnerable adult is expected.

If passed, the Act would require that the Securities and Exchange Commission make regulatory recommendations to prevent the financial exploitation of elderly and vulnerable adults. The Act would provide financial firms with greater comfort that they can take action to halt suspicious transactions while further investigation occurs.

This bipartisan Act is important for the future of protecting the elderly and vulnerable adults while providing the financial industry better tools to address suspected financial exploitation.