

Fiduciary Fall Out

Updates From Five Fairly Recent Texas Opinions

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Case 1: Jurisdictional Jungle.

In re Guardianship of Gibbs; Fort Worth Court of Appeals; April 3, 2008:

Short Summary:

A trust provided for distributions to the primary beneficiary (Mom) and ultimate beneficiaries (4 kids) and allowed that if Mom & 3 of 4 kids agreed, funds could be removed from the trust for Mom's benefit. Prior to and in fear of Y2K, Mom and 3 kids signed written authorizations to withdraw \$1mil and use \$700k to purchase gold coins and the balance for food and other items to prepare for Y2K. 4th child was not consulted and in Sept. 2000 brought suit in probate court for breach of fiduciary duties related to removal of the trust funds. In May 2001 4th child also brought an application for temporary guardianship over Mom's estate in probate court. In June, 4th Child applied to convert the temporary guardianship to a permanent one; however, the application was not contested until after the 60 duration of the temporary guardianship ran. In October the court transferred the breach of fiduciary duty case as ancillary to the guardianship action. At trial of the breach of fiduciary duty suit, the other 3 children did not attend, and the court entered a more than \$1mil verdict against the children and modified the trust to remove the other 3 children as trust beneficiaries. The 3 children appealed. On appeal, the Court of Appeals found that the fiduciary duty suit did not fit within the laundry list of actions the court had jurisdiction of under Section 115.001 of the trust act, and found that because the temporary guardianship had expired, the application to convert it to a permanent guardianship was essentially moot. Therefore, the court was without jurisdiction to hear the breach of fiduciary duty case or enter judgment on it, and the judgment was void.

Lessons Learned:

1. Failure to follow the proper procedure wiped out a million dollar judgment.
2. Jurisdiction in Texas Probate cases remains a jungle with punji pits for the unwary.
3. The laundry list in 115.001 of the trust act is an exclusive list of actions concerning trusts over which a district court has jurisdiction.
4. The time deadlines regarding temporary guardianships hold fast unless a permanent guardianship is contested within 60 days of the temporary guardianship or a new temporary guardian is appointed under Section 875 of the probate code.

Case 2: Removal Rectifies Conflict Chaos.

In re Estate of Kappus; Tyler Court of Appeals; November 30, 2007.

Short Summary:

2 brothers and a father formed Kappus Farms. After father died, the 2 brothers owned the property together, and evidence indicated James owned about 60% and John owned about 40%, although there were no formal records and this was based on various farm improvements over time by each brother. Brother 1, James, had a will naming Brother 2, John, as executor and testamentary trustee. James left his assets to his 2 children via the will and testamentary trust. After James' death, John was appointed executor and took steps to sell Kappus Farms and split the proceeds equally between himself and the trust. James' Ex-wife (mother of the 2 children) brought suit on behalf of the children to remove John as executor and trustee on the basis of conflict of interest. Under section 149c of the probate code, an executor may be removed for gross misconduct or gross mismanagement in the performance of his duties. John's position as to his ownership in the interest of the farm was adverse to the estate's position, creating a conflict requiring removal. Further under section 37 of the Probate Code, title to property devised to a testamentary trust vests immediately upon the testator's death absent "unambiguous intent that the assets not vest at moment of death." Because the assets vested, the court further considered whether John should be removed as trustee for other good cause under section 113.082 of the trust act. John's asserted ownership of property claimed by the trust was "an attempted appropriation in violation of fiduciary duty" and a conflict of interest warranting removal.

Lessons Learned:

1. On the drafting front, immediate vesting of property in a testamentary trust can be avoided if desired and proper wording is used.
2. A conflict of interest can serve as grounds for removal of an executor.
3. A conflict of interest can serve as "other good cause" for removal of a trustee.

Case 3: Contingency Causes Standing Shortfall

Moon v. Lesikar; Houston 14th Court of Appeals; July 10, 2007.

Short Summary:

Dad creates Family Living Trust and funds it in part with stock worth around \$193k. Dad was trustee and income beneficiary for life, and reserved the right to revoke or amend the trust agreement. Son and Daughter were remainder beneficiaries. During his life, Dad added other assets to the trust and also sold the stock to a trust for his Son's 2 children (Dad's grandchildren) for \$2k (massively less than actual value). After death, Daughter brought for breach of fiduciary duty regarding the sale of stock by the Family Trust to the Grandchild trust for inadequate price. The trial court granted summary judgment against Daughter based on lack of standing, and the Court of Appeals affirmed. The Court of Appeals said it was an issue of first impression in Texas whether a contingent beneficiary can complain of a transaction by the settlor of a revocable trust when the act is taken prior to the vesting of her interest by the death of the settlor. The Court concluded that because Dad was the settlor with power to revoke the trust, the sole beneficiary while alive, and trustee with the power to amend, Daughter had no standing to complain of Dad's disposition of Family Trust Assets.

Lesson Learned:

Unless the lifetime disposition violates the terms of the trust (e.g. The trust has become irrevocable after a spousal death) it does not appear that a contingent beneficiary of a revocable family trust can complain of a transaction by the settlor when the act occurs prior to the vesting of the contingent interest.

Case 4: Iffy Immunity Applies to Appointments

Alpert v. Gerstner; Houston 1st Court of Appeals; August 31, 2006.

Short Summary:

Attorney appointed receiver over 3 trusts and her law firm were sued for breach of fiduciary duty for failing to preserve and protect assets of the trust. Receiver filed for summary judgment on the basis of judicial immunity in her capacity as court appointed receiver. Law firm filed for summary judgment on the basis of no duty owed by attorney for receiver/trustee to beneficiaries of trust. The order authorizing the hiring of the law firm, however, also provided that the firm was hired "to assist the Receiver in the administration of her duties." In considering the judicial immunity claim, the court determined that whether a court appointed receiver is entitled to judicial immunity is a case of first impression, and considered other similar officer of the court roles. The Court noted a Bankruptcy trustee is entitled to immunity; and a guardian ad litem under the Family code is entitled to immunity for acts within the scope of the appointment as an extension of the Court; but a guardian ad litem for a minor settlement hearing does not have immunity for breach of duty to the minor; a court appointed guardian does not have immunity for managing the estate of the ward; and a court appointed trustee was not entitled to judicial immunity relating to trust investments. Therefore the Court found that a receiver is not entitled to immunity for breach of fiduciary duties to beneficiaries relating to investment/management of the assets of the trusts. The Court of Appeals further found that because the order hiring the lawyers for the receiver authorized them to "assist in the administration of the trusts" a fact question existed as to whether the lawyers solely performed services as attorneys for the receiver or also provided receivership services and owed duties to the trust beneficiaries.

Lessons Learned:

1. If you represent a court appointee, make sure both your engagement letter and the order authorizing your hire limits the scope of the engagement to representation of the appointee; otherwise, as an attorney, you may owe duties to the recipient of the appointee's services.
2. A bankruptcy trustee is entitled to judicial immunity.
3. A guardian ad litem under the Family code is entitled to immunity for acts within the scope of the appointment.
4. A guardian ad litem for a minor settlement hearing does not have immunity for breach of duty to the minor.
5. A court appointed guardian does not have immunity for managing the ward's estate.
6. A court appointed trustee does not have judicial immunity relating to trust investments.
7. A court appointed receiver does not have judicial immunity for investment/management of receivership/trust assets.

Case 5: Settlor Soars, Trustee Tanks

Alpert v. Riley; Houston First Court of Appeals; June 5, 2008

Short Summary:

This is the second Alpert opinion (see Case 4, above). Robert Alpert set up 3 trusts for his two sons. Alpert was settlor only, not a trustee. Among other terms, the trusts provided that the trustee would not be entitled to compensation. Mark Riley served as an attorney for Alpert for about 4 years, including as legal counsel for the trusts. In 1998 the relationship between Riley and Alpert soured and Riley later claimed he was the trustee of all 3 trusts -- which Alpert and the beneficiaries denied. Riley sued Alpert for breaches of fiduciary duty related to transactions the trusts made, and the beneficiaries sued Riley for breaches of fiduciary duty. The trial court (Judge Mike Wood) ruled on summary judgment that Riley was the trustee of all 3 trusts, that Alpert violated fiduciary duty; and held a trial on the breach of duty claims. At trial, the jury found Riley had breached his fiduciary duty but found no damages. The judge disregarded the breach answer. The jury also found significant damages against Alpert (about \$2.5mil) for breach of fiduciary duty. The judge also awarded more than \$1.5 mil in attorneys fees to Riley and denied the \$162k in fees that the jury awarded the beneficiaries against Riley. The trial court also awarded Riley trustee compensation. After the judgment and before the appeal, under a new provision enacted by the Texas Legislature, the beneficiaries made a written request that Riley no longer pursue the claims against Alpert; however, Riley continued his pursuit.

On Appeal, the Court found Riley was not the trustee of one of the trusts as a matter of law and that a fact question precluded summary judgment as to the other two trusts; that Alpert as settlor had no fiduciary duty as to the management of the trusts, only the trustee does; that Riley's breach of duty should not have been disregarded; that the award of attorneys fees to Riley and the denial of fees to the beneficiaries was reversed for further consideration by the trial court; that Riley was not entitled to trustee compensation and that under the new statute, Riley had no choice but to heed the beneficiaries wishes and stop prosecuting the claims against Alpert upon receipt of their written opposition.

Lessons Learned:

1. Trust instruments are interpreted like contracts, and the trust agreement's language prevails over the terms of the trust code in most instances. If the trust says "No Trustee compensation or commissions" then it means "No Trustee compensation or commissions."
2. A settlor has no duty to manage trust property, and no fiduciary duty to beneficiaries once the trust is created and accepted by the trustee. The trustee alone is liable for breach of fiduciary duty if he allows the settlor to mismanage property to the detriment of the trust.
3. A trustee has no standing to sue a settlor for a purported breach of fiduciary duty (but beware a *Kinzbach* claim for the settlor's knowingly participating in or aiding or abetting a breach of fiduciary duty).
4. Under Section 113.028 (a new Texas Property Code section), a trustee may not prosecute a claim for damages against a non-beneficiary if all of the beneficiaries give written notice of their opposition to the trustee doing so.