

Does a trust beneficiary incur any personal liability?

As a general rule, one assumes no personal liability when one becomes a trust beneficiary. There are some exceptions, however. Charles E. Rounds, Jr. explains in Section 5.6 of *Loring and Rounds: A Trustee's Handbook* (2012), which is reproduced below.

## §5.6 Duties and Liabilities of the Beneficiary

[Reprinted from Charles E. Rounds, Jr., et al, *Loring and Rounds: A Trustee's Handbook* (2012), pages 396-400, Wolters Kluwer; toll free ordering: 1-800-638-8437]

*The trustee is bound to know what his duty is, and can not throw upon the cestui que trust the obligation of telling him what such duty is. Mere knowledge and noninterference by the cestui que trust before his interest has come into possession do not always bind him as acquiescing in the breach of trust.*<sup>1</sup>

*The beneficiary does not have title to the underlying trust property.* Except perhaps in certain cases where the beneficiary controls the trustee, the beneficiary will not be held liable as the constructive owner of the *underlying trust property*.<sup>2</sup> Thus in matters involving the trust estate and third parties, the beneficiary is liable neither in contract<sup>3</sup> nor in tort,<sup>4</sup> neither criminally for a nuisance on the trust property,<sup>5</sup> or for a trustee's unlawful acts of discrimination,<sup>6</sup> nor as a stockholder.<sup>7</sup>

*Ownership of the equitable interest generally does not bring with it liabilities.* With the possible exception of those trusts under which the beneficiary for all intents and purposes controls the trustee (e.g., the revocable inter vivos trust, the realty trust, or the nominee trust), the beneficiary also incurs no liabilities arising inherently out of *ownership of the equitable or beneficial interest*, except when it comes to taxation.<sup>8</sup>

*The trustee is not an agent of the beneficiary.*<sup>9</sup> In fact, the trustee's duty not to delegate the administration of the trust could well be implicated if the trustee without authority were to behave

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<sup>1</sup>White v. Sherman, 168 Ill. 589, 606, 48 N.E. 128, 132 (1897).

<sup>2</sup>See 3 Scott on Trusts §§274, 274.1.

<sup>3</sup>See 3 Scott on Trusts §275.

<sup>4</sup>See 3 Scott on Trusts §276.

<sup>5</sup>See 3 Scott on Trusts §265.3.

<sup>6</sup>See Bogert, Trusts and Trustees §731.

<sup>7</sup>See 3A Scott on Trusts §265.2.

<sup>8</sup>4 Scott & Ascher §22.6 (Indemnity from Beneficiaries); 3A Scott on Trusts §274. See generally §§7.3.3 of this handbook (trustee's liability as legal owner in tort to nonbeneficiaries) and 9.6 of this handbook (trusts that resemble corporations or agencies).

<sup>9</sup>See, e.g., Buck v. Haas, 180 La. 188, 156 So. 217 (1934). But see Uniform Trust Code §108(e) (available on the Internet at <<http://www.law.upenn.edu/bll/ulc/ulc.htm>>) (providing that a trustee may not transfer a trust's principal place of administration over the objections of a qualified beneficiary without court approval).

as if he were the beneficiary's agent.<sup>10</sup> In the absence of agreement, the beneficiary is not personally bound to indemnify the trustee for trust administration expenses.<sup>11</sup> The beneficiary may voluntarily undertake to make himself or herself liable to the trustee, *e.g.*, by furnishing funds to enable the trustee to improve the trust estate or by litigating in order to collect insurance proceeds.<sup>12</sup> In England, on the other hand, the beneficiary in some cases may be personally bound to indemnify the trustee to the extent there are insufficient assets in the trust estate to do so.<sup>13</sup>

*Beneficiary generally must return overpayments.* Both in England and the United States, the beneficiary would generally be liable to indemnify the trustee for liability occasioned by overpayment or misdelivery of the trust property *to the beneficiary*.<sup>14</sup> Otherwise, the beneficiary would be unjustly enriched.<sup>15</sup> If a beneficiary wrongfully deals with trust property, any loss can be made up from the beneficiary's interest;<sup>16</sup> in the case of overpayment, as noted above, the beneficiary may be personally liable.<sup>17</sup> "One who seeks equity must do equity."<sup>18</sup> Where an innocent overpayment has been made, there may be a change of position by the beneficiary, however, that makes it inequitable to compel repayment.<sup>19</sup> A trustee makes distribution at his peril: An overpayment that is not repaid by the beneficiary is a personal obligation of the trustee.<sup>20</sup> "A beneficiary of a trust that is determined to have been invalid is liable to return any distribution received."<sup>21</sup>

*Beneficiary may not knowingly participate in a breach of trust.* A beneficiary is liable to the same extent as any other person for participation or collusion in a breach of trust.<sup>22</sup> "Although

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<sup>10</sup>See generally 3 Scott & Ascher §17.3.2 (citing to Matter of Osborn, 299 N.Y.S. 593 (App. Div. 1937)).

<sup>11</sup>See Bogert, Trusts and Trustees §718; 4 Scott & Ascher §22.6.

<sup>12</sup>Restatement (Second) of Trusts §278 (1959).

<sup>13</sup>See generally 4 Scott & Ascher §22.6 (Indemnity from Beneficiaries)

<sup>14</sup>4 Scott & Ascher §22.6.1 (When Trust Estate Has Already Been Conveyed).

<sup>15</sup>Restatement of Restitution §163 ("Where the owner of property transfers it as a result of mistake of such a character that he is entitled to restitution, the transferee holds the property upon a constructive trust for him").

<sup>16</sup>Restatement (Second) of Trusts §253 (1959); 4 Scott & Ascher §25.2 (Liability of Beneficiary to Trust Estate).

<sup>17</sup>Restatement (Second) of Trusts §254 (1959); Restatement of Restitution §163 (1937) (U.S.); 4 Scott & Ascher §§22.6.1 (U.S.) (When Trust Estate Has Already Been Conveyed), 25.2 (Liability of Beneficiary to Trust Estate) (U.S.), 25.2.4 (Beneficiary Who Receives Overpayment) (U.S.); Lewin on Trusts ¶42-04 through ¶42-10 (England) (discussing a trustee's common law right of recovery and equitable right of recoupment).

<sup>18</sup>See generally 4 Scott & Ascher §25.2 (Liability of Beneficiary to Trust Estate); §8.12 of this handbook (containing a list of equity maxims); Snell's Equity ¶5-09.

<sup>19</sup>4 Scott & Ascher §25.2.4.1 (Change of Position); Restatement (Second) of Trusts §254 (1959); Restatement of Restitution §178 (Change of Position) (1937). *But see* First Union Nat'l Bank v. McGill, 684 So. 2d 845 (Fla. Ct. App. 1996) (trustee's improper allocation of capital gains to the income account shall be made up by a remedial allocation to principal of future income payments, rather than by surcharging the trustee).

<sup>20</sup>See generally 4 Scott & Ascher §§24.31 (Liability for Incorrect Distributions), 25.2.4.2 (Rights of Trustee and Other Beneficiaries).

<sup>21</sup>Uniform Trust Code §604(c) (available on the Internet at <<http://www.law.upenn.edu/bll/ulc/ulc.htm>>). See also 4 Scott & Ascher §25.2 (Liability of Beneficiary to Trust Estate).

<sup>22</sup>Bogert, Trusts and Trustees §256; 4 Scott & Ascher §§25.2 (Liability of Beneficiary to Trust Estate), 25.2.6 (Beneficiary Who Consents to or Participates in Breach of Trust), 25.2.6.3

there is not the same fiduciary relationship between trust beneficiaries as there is between them and the trustee, there is enough of a fiduciary element in their relationship to make it inequitable for one to seek to obtain an advantage over another.”<sup>23</sup> The English cases are in accord.<sup>24</sup> If beneficiary *X* persuades the trustee improperly to lend or distribute to him trust property, *X* may be liable to beneficiaries *Y* and *Z*.<sup>25</sup> *X*'s own interest in the trust estate may be subjected to an equitable lien in their favor.<sup>26</sup> The beneficiary would be ill advised to instruct the trustee in matters concerning management of the trust estate.<sup>27</sup>

*The trustee takes directions from the beneficiary at his peril, unless the terms of the trust provide otherwise.* The trustee would be equally ill advised to blindly follow the beneficiary's instructions.<sup>28</sup> The trustee is in no way excused from liability merely because some of the beneficiaries insisted upon an improper action—except perhaps as to a claim presented by those who did the insisting.<sup>29</sup> Moreover, as noted, the interfering beneficiaries may be held to have colluded in the breach of trust.<sup>30</sup>

*Beneficiary's liability is generally limited.* The beneficiary may not be forced to contribute personal funds in order to prevent the trust property from being taken by foreclosure.<sup>31</sup> Nor is the trustee “entitled to a charge on the beneficiary's interest in the trust to secure a liability of the beneficiary to the trustee not connected with the administration of the trust, unless the beneficiary contracts to give him such a charge.”<sup>32</sup> Neither is a third party who owes a contractual obligation to the trustee, *e.g.*, the issuer of a bond or an insurance policy that is an asset of the trust, generally entitled, in lieu of making payments to the trustee, to set off a personal claim that the third party has against the beneficiary.<sup>33</sup>

*Beneficiary may voluntarily assume trust liabilities.* A trust beneficiary, of course, may voluntarily enter into an enforceable contract to pay money or property into the trust (or back into

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(Participation by Beneficiary in Breach of Trust). *See generally* §5.4.1.8 of this handbook (right and standing of beneficiary to proceed in stead of trustee against those with whom the trustee has contracted, against tortfeasors, and against his agents, *i.e.*, against third parties).

<sup>23</sup>4 Scott & Ascher §25.3 (Beneficiary's Duty to Other Beneficiaries).

<sup>24</sup>Lewin on Trusts ¶40-06 (England).

<sup>25</sup>Bogert, Trusts and Trustees §256; 4 Scott & Ascher §§25.2 (Liability of Beneficiary to Trust Estate), 25.2.4.2 (Rights of Trustee and Other Beneficiaries).

<sup>26</sup>Bogert, Trusts and Trustees §256; 4 Scott & Ascher §§25.2 (Liability of Beneficiary to Trust Estate), 25.2.3 (Beneficiary Who Deals Wrongfully with Trust Property).

<sup>27</sup>Bogert, Trusts and Trustees §216; 4 Scott & Ascher §25.2 (Liability of Beneficiary to Trust Estate).

<sup>28</sup>Bogert, Trusts and Trustees §256(2) (One Beneficiary's Consent to a Breach of Trust Will Not Relieve Trustee from Liability to the Other Beneficiaries); 1 Scott on Trusts §8 (Trustee Not an Agent of the Beneficiary). *See also* Restatement (Third) of Trusts §80 cmt. b (noting that the trustee can properly take into account information or suggestions furnished by a beneficiary but then “must exercise independent, prudent, and impartial fiduciary judgment on the matters involved”).

<sup>29</sup>Restatement (Second) of Trusts §216 cmt. g (1959).

<sup>30</sup>Restatement (Second) of Trusts §256; 4 Scott & Ascher §25.2 (Liability of Beneficiary to Trust Estate).

<sup>31</sup>*See* 2A Scott on Trusts §176.

<sup>32</sup>Restatement (Second) of Trusts §250 (1959; 4 Scott & Ascher §25.1 (Liability of Beneficiary to Trustee Individually).

<sup>33</sup>5 Scott & Ascher §32.2 (Set-Off of Claim of Third Person Against Beneficiary).

the trust in the case of a loan or advancement)<sup>34</sup> in which case the beneficiary's interest is subject to a charge for the amount of the obligation.<sup>35</sup> In spite of the public policy implications, even a beneficiary's agreement to indemnify the trustee against losses occasioned by a breach of trust *that the beneficiary had asked the trustee to commit* may be enforceable.<sup>36</sup> Also, if a beneficiary engages in frivolous litigation against the trustee or the trust, that beneficiary's interest may be charged with payment of the costs.<sup>37</sup>

*The litigious nuisance beneficiary.* In litigation pertaining to a trust, the court has discretion to order the trustee to reimburse the beneficiary from the trust estate for the beneficiary's reasonable legal fees and other litigation costs.<sup>38</sup> The litigation, however, must be indispensable to the proper administration of the trust or confer a benefit on the beneficiary class.<sup>39</sup> If the trustee is found to be personally at fault, the trustee may then be required to reimburse the trust estate out of his own funds for what was paid out to the beneficiary.<sup>40</sup> If a trustee has prevailed in a suit for breach of trust, he is entitled to be indemnified from the trust estate for his litigation costs.<sup>41</sup> If the suit was brought vexatiously, obdurately, or in bad faith by the beneficiary, the trustee may have a fiduciary duty to the other beneficiaries to bring an action against the beneficiary to force the beneficiary to reimburse the trust estate for the trustee's attorneys' fees and other litigation costs.<sup>42</sup> Circumstances even may warrant that an action be brought on behalf of the trust against the nuisance beneficiary's counsel as well.<sup>43</sup>

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<sup>34</sup>See generally 4 Scott & Ascher §25.2.5 (Beneficiary Who Receives Advance or Loan of Trust Funds). *But see* 4 Scott & Ascher §25.2.5.1 (Advances to Beneficiary of Spendthrift Trust).

<sup>35</sup>4 Scott & Ascher §25.2.2 (Beneficiary's Contractual Obligations to Trust).

<sup>36</sup>4 Scott & Ascher §25.2.6.2 (When Consenting Beneficiary Agrees to Indemnify Trustee).

<sup>37</sup>See 3 Scott on Trusts §188.4 n.13 and accompanying text. *See generally* §8.13 of this handbook (in litigation pertaining to a trust, when is the beneficiary entitled to reimbursement from the trust estate for legal fees).

<sup>38</sup>See generally §8.13 of this handbook (when the beneficiary may be entitled to be reimbursed from the trust estate for his or her legal fees).

<sup>39</sup>See generally §8.13 of this handbook (when the beneficiary may be entitled to be reimbursed from the trust estate for his or her legal fees).

<sup>40</sup>See generally §7.2.3.7 of this handbook (assessment of attorneys' fees and other costs against the trustee personally).

<sup>41</sup>See generally §3.5.2.3 of this handbook (the trustee's right to exoneration and reimbursement).

<sup>42</sup>See generally §3.5.2.3 of this handbook (tagging the nuisance beneficiary with all litigation costs).

<sup>43</sup>See, e.g., Pederson Trust, 757 N.W.2d 740 (N.D., 2008) (beneficiary and his counsel held joint and severally liable for the trustee's attorneys' fees).