

Title

Recourse at law or in equity of trust beneficiary who is dissatisfied with trustee's proposed settlement with insurance company of property-damage claim

Text

Assume entrusted property that has been duly insured by the trustee suffers damage through no fault of the trustee. A current beneficiary, though, is unhappy with the trustee's proposed nonjudicial accommodation with the insurance company. The beneficiary requests that trustee assign its contractual rights against the insurance company to the beneficiary personally so that the beneficiary may take it upon himself to bring suit against the insurance company, with any recovery to be remitted to the trust estate. The trustee declines to execute such an assignment. What recourse, if any, should the beneficiary have at law and/or in equity?

If it would be imprudent/unreasonable for the trustee to further pursue the insurance company, then the trustee should have no duty to assign the contractual rights to the beneficiary. See §[6.2.1.3](#) of *Loring and Rounds: A Trustee's Handbook*, which is reproduced in its entirety in Appendix A below.

On the other hand, if it would be imprudent/unreasonable for the trustee to enter into the proposed settlement with the insurance company in the first place then the beneficiary would have recourse in equity directly against the trustee personally. *Id.* But what if the trustee were, say, judgement-proof? The beneficiary, *qua* beneficiary, then would have a right under equitable principles to bring an action at law on the contract directly against the insurance company on behalf of the trust (and at trust expense, if successful), provided the trustee had unreasonably declined to do so. See §[5.4.1.8](#) of Handbook, which is reproduced in relevant parts in Appendix B below. In other words, the trustee's unreasonable forbearance could effect what amounts to an involuntary equitable assignment of the contractual rights to the beneficiary, an assignment that the insurance company should be in no position to defeat.

As to the trustee in the face of its reasonable forbearance assigning anyway the contractual rights to the beneficiary, what harm could that possibly do? There are several reasons why the trustee should think twice before doing something like that. The first is doctrinal: The beneficiary becomes a fiduciary agent of the trustee, which brings with it a duty on the part of the trustee to monitor/oversee the agent's activities. The second is practical: Who is to bear the burden of the trustee's attendant legal fees, monitoring costs, and other such expenses? The trustee personally? The trust estate? The beneficiary? At the very minimum, the trustee is likely to be made a nominal party in the beneficiary-agent's litigation against the insurance company. No way the trust estate the remaindermen will say.

Practice tip: Is the beneficiary entitled to principal distributions in the discretion of trustee? If so, a discretionary principal distribution of contractual rights possessed by the trustee as against the insurance company might be worth considering, assuming to do so would be within the trustee's discretionary authority. That way the trustee and the beneficiary can go about their separate ways with respect to the matter no longer constrained by the fiduciary principle.

Appendix A

§6.2.1.3 Duty to Protect and Preserve Trust Property; Duty to Enforce Claims; Duty to Defend Actions [from *Loring and Rounds: A Trustee's Handbook* (2021)].

*To protect the beneficiary against excessive costs, the trustee should also be alert to adjusting compensation for functions that the trustee has delegated to others.*¹⁰¹

*If mutual fund firms ran gas stations, the fees would be posted in tiny letters on the bathroom ceiling.*¹⁰²

Introduction. Except for the rare case where abandonment of an item of trust property serves the interest of the beneficiaries and is in furtherance of the trust's purposes,¹⁰³ the trustee is under a duty to take all reasonable steps to protect¹⁰⁴ and preserve/conservate the trust property.¹⁰⁵ Indenture trustees are no exception.¹⁰⁶ The reasonable costs of doing so are a legitimate trust expense.¹⁰⁷ This duty is not delegable.¹⁰⁸ A necessary part of this general duty encompasses vigilant protection of the trust property against deterioration or loss.¹⁰⁹ The trustee could be liable, for example, if he permitted stock subscription rights to expire¹¹⁰ or an entrusted life insurance

¹⁰¹UTC §805 cmt.

¹⁰²Charles Stein, *Only Scandal in High Fees Is Ignorance*, Boston Globe, Dec. 14, 2003, at p. G5.

¹⁰³See Restatement (Third) of Trusts §86 cmt. f.

¹⁰⁴Restatement (Third) of Trusts §76(2)(b). See, e.g., S. Leinberg & A. Gibbons, *Performing Due Diligence With Respect to Life Insurance Trusts Is Crucial*, 30 Estate Planning 748 (2003) (discussing the trustee's duty of due diligence when the trust is funded with contractual rights incident to a life insurance or annuity contract).

¹⁰⁵See Bogert §582; 3 Scott and Ascher §§17.8, 18.1.2.1; 2A Scott on Trusts §176; Lewin ¶34-23 through ¶34-29 (England). See also UTC §809.

¹⁰⁶Bogert §250, n.45. See generally §9.31 of this handbook (corporate trusts; trusts to secure creditors; the Trust Indenture Act of 1939; protecting bondholders).

¹⁰⁷See generally §3.5.2.3 of this handbook (trustee's equitable right to exoneration and reimbursement from the trust estate); 3 Scott & Ascher §18.1.2.1 (Preservation of the Trust Property).

¹⁰⁸See generally 2A Scott on Trusts §171.

¹⁰⁹See Restatement (Second) of Trusts §176 cmts. b, c; 3 Scott & Ascher §17.8. See also *United States v. White Mt. Apache Tribe*, 537 U.S. 465, 475–476 (2003).

¹¹⁰See 3 Scott & Ascher §17.8; 2A Scott on Trusts §176 n.28 and accompanying text.

contract to lapse due to premium nonpayment¹¹¹ or the key to a “wallet” of cryptocurrency to be lost or stolen.¹¹² Tax penalties or obligations unreasonably incurred, *e.g.*, as a result of the trustee’s negligence, are a personal expense of the trustee.¹¹³ In order to avoid the underpayment or overpayment of capital gains taxes, it is critical that the trustee keep proper track of the tax basis/cost of each item of trust property, a topic we take up in §10.3 of this handbook.

Unwarranted administrative costs. Administrative costs should be reasonable in relation to the trust property, the purposes of the trust, and the skills of the trustee.¹¹⁴ “If a trustee incurs a greater expense that is reasonable, the trustee cannot charge the trust estate with the excess.”¹¹⁵ The costs of the trustee’s unwarranted litigiousness, for example, are not reimbursable.¹¹⁶ Creditors’ claims should not be satisfied from trust assets unnecessarily.¹¹⁷ Public policy dictates that the terms of a trust may go only so far in “relaxing” this general duty to preserve the trust property.¹¹⁸ On the other hand, a trustee is not an insurer: “A trustee has a duty to use reasonable care and skill to preserve the trust property. The applicable standard is that of a person of ordinary prudence. If the trust property is lost or destroyed or declines in value, the trustee is not subject to

¹¹¹*See, e.g., Rafert v. Meyer*, 859 N.W.2d 332 (Neb. 2015). That having been said, it is generally the case that the trustee would have no duty to pay the premium with his personal funds.

¹¹²*See generally* §8.18 of this handbook (trustees transacting or investing in cryptocurrencies).

¹¹³*See generally* 3 Scott & Ascher §18.1.2.6 (When Trustee Improperly Incurs Expense). *Cf. McCormick v. Cox*, 118 So. 3d 980 (Fla. Dist. Ct. App. 2013) (the appellate court upholding a finding of the trial court that the trustee’s negligent failure to correct the undervaluation of the trust’s sole asset, a golf course, via an amended estate tax return necessitated a 1031 like-kind exchange transaction, at an additional cost to the trust of \$2,146,812.00, so as to avoid “an immediate and adverse capital gain tax to the...trust and beneficiaries”).

¹¹⁴UTC §805. *Cf. The Unif. Prudent Management of Institutional Funds Act §3(c)(1) (UPMIFA)* (imposing on an institution a duty to incur only costs that are appropriate and reasonable).

¹¹⁵3 Scott & Ascher §18.1.2.6 (When Trustee Improperly Incurs Expense). *See, e.g., McCormick v. Cox*, 118 So. 3d 980, 982 (Fla. Dist. Ct. App. 2013) (upholding a finding of the trial court that legal fees paid by the trustee to trust counsel’s law firm were “substantially unreasonable and unsupported by the evidence”). The court also found that counsel having participated in the trustee’s breach of trust must share the trustee’s liability. *See generally* §7.2.9 of this handbook (trust counsel liability).

¹¹⁶*See generally* 3 Scott & Ascher §18.1.2.6 (When Trustee Improperly Incurs Expense).

¹¹⁷*See, e.g., Dobler v. Arluk Med. Ctr. Indus. Grp.*, 107 Cal. Rptr. 2d 478 (Ct. App. 2001), *aff’d in subsequent appeal*, 11 Cal. Rptr. 3d 194 (Ct. App. 2004) (in which a trustee of a revocable trust successfully avoided having to satisfy from trust assets the claims of the postmortem creditors of the deceased settlor by transferring assets to the trust beneficiaries before the claims were reduced to judgment). *See generally* 3 Scott & Ascher §17.10 (Duty to Defend Actions).

¹¹⁸3 Scott & Ascher §17.8.

surcharge unless the trustee has failed to exercise reasonable care and skill.”¹¹⁹

Below-market sales. A sale by a trustee of trust property to a third party for less than its market value¹²⁰ is not protecting the trust property.¹²¹ “Conceivably, a sale at the prevailing market price might be improper if, owing to economic conditions or the conditions of the market in question, prices are depressed.”¹²²

Unless it is imprudent to do so under the circumstances, or the trust terms provide otherwise, a parcel of trust real estate should be listed for sale on the open market¹²³ with independent brokers, *i.e.*, brokers who are free of conflicts of interest, and only after the trustee has obtained at least one current appraisal by an independent competent appraiser¹²⁴ who has employed one or more of the

¹¹⁹3 Scott & Ascher §17.8.

¹²⁰Market value is “the most probable price which property should bring in a competitive and open market under all conditions requisite for a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus.” Glossary of the Uniform Standards of Professional Appraisal Practice (2000 ed.). “Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under certain conditions whereby: (1) buyer and seller are typically motivated; (2) both parties are well informed or well advised, and acting in what they consider their best interests [or in the case of a trustee, the best interests of the beneficiaries]; (3) a reasonable time is allowed for exposure in the open market; (4) payment is made in terms of cash in United States dollars or in terms of financial arrangements comparable thereto; and (5) the price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.” Glossary of the Uniform Standards of Professional Appraisal Practice (2000 ed.). Treas. Reg. §25.2512-1 has a similar definition of fair market value for federal gift tax purposes:

“The value of...[gifted]...property is the price at which such property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of relevant facts. The value of a particular item of property is not the price that a forced sale of the property would produce. Nor is the fair market value of an item of property the sale price in a market other than that in which such item is most commonly sold to the public, taking into account the location of the item wherever appropriate....”

¹²¹3 Scott & Ascher §18.1.4.4 (confirming that a trustee who sells trust property at an unreasonably low price is liable for the loss).

¹²²4 Scott & Ascher §24.11.4 (When Trustee Has Power of Sale).

¹²³On the trustee’s duty to “test the market,” see *Rippey v. Denver U.S. Nat’l Bank*, 273 F. Supp. 718 (D. Colo. 1967).

¹²⁴See, *e.g.*, *Lincoln Nat’l Bank & Trust Co. v. Shriners Hosps. for Crippled Children*, 588 N.E.2d 597 (Ind. Ct. App. 1992); *Allard v. Pac. Nat’l Bank*, 99 Wash. 2d 394, 405, 663 P.2d 104, 111 (1983); *Belcher v. Birmingham Trust Nat’l Bank*, 348 F. Supp. 61, 158 (N.D. Ala. 1968).

following standard valuation methods as appropriate: Sales Comparison,¹²⁵ Cost,¹²⁶ and Income Capitalization.¹²⁷ The trustee who sells entrusted real estate that has not been duly appraised is asking for trouble.¹

Receiving a secured promissory note in lieu of cash is generally permissible, provided the note standing on its own two feet would be a suitable investment for the particular trust.¹²⁸ “In some circumstances, however, it may be proper for a trustee to accept from the buyer a note or other asset of a type or in an amount that the trustee would not otherwise acquire for the trust portfolio when it is prudent under the circumstance to do so, considering any special advantages of the sale opportunity along with the tax as well as investment aspects of the transaction.”¹²⁹

Relocating the trust’s situs. If the location of the trust’s principal place of administration puts the trust property at unreasonable risk, the trustee may have a duty to transfer the trusteeship to someone who is in a position to administer the trust at a place appropriate to its sound, efficient management, at least at one time the Uniform *Probate* Code had so provided.¹³⁰ When it comes to taxation, divorce, and creditor access, some jurisdictions are more favorable to the interests of trust beneficiaries than others. New York, for example, imposes a tax on undistributed dividends and capital gains. Delaware, on the other hand, does not. Alaska, unlike many jurisdictions, will enforce the spendthrift provisions of certain self-settled trusts. The general subject of conflict of laws is taken up in §8.5 of this handbook; the general subject of judicial jurisdiction in §8.40 of this handbook.

A trustee may have a duty to move the situs of the trust if to do so would substantially further the interests of the beneficiaries, would not be in contravention of the terms of the trust, and would be both possible and practical.¹³¹ The Uniform *Trust* Code is generally in accord.¹³² If such a move

¹²⁵Comparative analysis of the subject with other similar properties that have recently sold and for which the sales price and terms are known.

¹²⁶Land value added to the estimated reproduction cost new of the improvements less depreciation from all causes.

¹²⁷Analysis of income and expenses and conversion of the net incomes stream(s) into an estimate of value.

¹ See, e.g., Living Trust Agreement of Morningstar, 136 N.E.3d 1139 (Ind.App. 2019).

¹²⁸Restatement (Third) of Trusts §86 cmt. c(2). See generally §6.2.2.1 of this hand book (the *Harvard College* prudent man rule and its progeny).

¹²⁹Restatement (Third) of Trusts §86 cmt. c(2). See also 3 Scott & Ascher §18.1.4.5 (Power to Sell on Credit).

¹³⁰UPC §7-305 [withdrawn].

¹³¹Restatement (Third) of Trusts §76 cmt. b(2).

¹³²UTC §108(b) (“A trustee is under a continuing duty to administer the trust at a place appropriate to its purposes, its administration, and the interests of the beneficiaries.”).

were only possible were the trustee to relinquish the trusteeship, then so be it.¹³³ On the other hand, “changes in the place of administration, location of beneficiaries, or other developments causing serious geographic inconvenience to the beneficiaries or to the administration of the trust” may be grounds for removal.¹³⁴

Section 7-101 of the UPC, now withdrawn, would have required a trustee to register the trust in an appropriate court at the trust’s principal place of administration. This registration requirement was in part designed to facilitate administratively the appropriate relocation of a trust’s principal place of administration by keeping court involvement in the process to a minimum.¹³⁵

All this having been said, changing trust situs may not be in the best interests of the beneficiaries, all things considered. The state in which the trust was established, for example, might attempt to continue to tax the income of the trust even after all the trustees and all the beneficiaries had moved elsewhere.¹³⁶ A trustee who is contemplating making a significant change in the place of administration of an inter vivos trust should so inform the beneficiaries and solicit their comments.¹³⁷ While they ordinarily would not have a power to veto the move, they should be given the opportunity in advance of the move to petition the court for instructions should they object to what is being contemplated.¹³⁸

Investing imprudently. It is implicit in the so-called Prudent Man Rule in all its manifestations, including the Restatement’s recently adopted *Prudent Investor Rule*, that the trustee, in investing the trust estate, must strive to protect trust principal from the ravages of inflation.¹³⁹

Transaction costs should be kept to a minimum.¹⁴⁰ The trustee intending to purchase mutual

¹³³Restatement (Third) of Trusts §76 cmt. b(2).

¹³⁴Restatement (Third) of Trusts §76 cmt. b(2); UPC §7-305 [withdrawn] (having provided that “[v]iews of adult beneficiaries shall be given weight in determining the suitability of the trustee and the place of administration”).

¹³⁵UPC, Part 1, Trust Registration, General Comment [relevant parts withdrawn].

¹³⁶See generally Bernard E. Jacob, *An Extended Presence, Interstate Style: First Note on a Theme from Saenz*, 30 Hofstra L. Rev. 1133 (2002) (considering claims of constitutional protection that ought to be erected against literal application of the “Founder-State Trust” concept).

¹³⁷Restatement (Third) of Trusts §76 cmt. b(2).

¹³⁸Restatement (Third) of Trusts §76 cmt. b(2).

¹³⁹See Restatement (Third) of Trusts §90 cmt. e [Restatement (Third) of Trusts: Prudent Investor Rule §227 cmt. e].

¹⁴⁰See, e.g., *Municipal Bonds: Tax Free Income vs. Trustee Obligation to Avoid Unwarranted Costs*, 33 ACTEC L.J. 195 (2008). While monitoring transaction costs is relatively easy when the trust assets are individually invested, it is another matter when the assets are mutual fund participations. Still, the trustee still has a duty to scrutinize a mutual fund’s cost structure, even if it is an index fund. See generally Luther J. Avery & Patrick J. Collins, *Managing Investment Expenses: Trustee Duty to Avoid*

fund shares through a broker, for example, must do so prudently. Whether A shares, B shares, or C shares are taken into the trust can make a difference to the trust's bottom line depending upon the given facts and circumstances, *e.g.*, the expected duration of the investment. With A shares, there is an initial sales commission and an annual 12b-1 fee in the range of 0.25 percent, which is over and above the fund's other annual expenses. With B shares, there is an annual 12b-1 fee of 1 percent and a back-end (exit) commission that declines the longer the shares are held. Eventually the B shares will convert into A shares, which have a lower 12b-1 fee structure. With C shares, there is an annual 12b-1 fee of 1 percent, but no upfront or back-end commission charges. "In the vast majority of cases, the B shares are never the most advantageous of the share classes."¹⁴¹ For a brief discussion of 12b-1 fees, see §8.10 of this handbook.

Tax liabilities should be prudently incurred if they must be incurred. The trustee must be aware that almost anything he does can have positive or negative tax consequences for the trust.¹⁴² The trustee's duty to keep track of the tax basis/cost of the trust property is discussed in §11.1 of this handbook.

Costs of unreasonably delegating tasks to agents. The duty not to incur unreasonable costs also applies when a trustee decides whether and how to delegate tasks to agents, including investment managers and attorneys.¹⁴³ "In deciding whether and how to delegate, the trustee must be alert to balancing projected benefits against the likely costs."¹⁴⁴ The trustee, for example, will want to ascertain to what extent, if at all, fees paid to investment advisors are a deductible expense for income tax purposes.¹⁴⁵ Even though a trustee has properly employed an attorney, only that portion of the legal fee that is reasonable under all of the circumstances is a legitimate trust

Unreasonable or Inappropriate Costs, 25 ACTEC Notes 123 (1999) (covering the following topics: The Unsophisticated Fiduciary and the Decision to Obtain Investment Expertise; Hiring a Professional Trustee; Seeking Asset Management Advice from a Broker; Costs of Investment Management Strategies; Range of Expenses for Managed Investment Funds; Commissions and Fees; Whether Expensive Investment Programs Produce Superior Returns; Market Impact and Liquidity Costs; and Taxes, Inflation and Turnover). *See also* Tom Lauricella, *This Is News? Fund Fees Are Too High, Study Says*, Wall St. J., Aug. 27, 2001, at C1, col. 5; Danny Hakim, *Index Fund Fees Are Not Created Equal*, N.Y. Times, Jan. 14, 2001, at BU8, col. 2.

¹⁴¹Jonathan Clements, *Why B Shares Deserve to Get an F: These Broker-Sold Funds Are a Bad Deal*, Wall St. J., July 2, 2003, at D1 (quoting Edward O'Neal, a finance professor at Wake Forest University in Winston-Salem, N.C.).

¹⁴²*See, e.g.*, Jonathan G. Blattmacher, *Put In Trust*, D-1, D-4 (1999) (suggesting that the rent-free use of property owned by a trust by its beneficiary does not result in imputed income to either the trust or the beneficiary). *See generally* Mark L. Ascher, *The Fiduciary Duty to Minimize Taxes*, 20 Real Prop. Prob. & Tr. J. 663 (1985).

¹⁴³UTC §805 cmt.; Restatement (Third) of Trusts §88 cmt. c.

¹⁴⁴UTC §805 cmt.

¹⁴⁵*See, e.g.*, Mellon Bank, N.A. v. United States, 47 Fed. Cl. 186 (Fed. Cl. 2000) (holding that income tax deduction for fees paid by trustee to outside investment advisors subject to two percent floor).

expense.¹⁴⁶ Any excess would be a personal obligation of the trustee.¹⁴⁷

Insuring the trust property. The trustee should insure the trust property to the extent it is reasonable to do so against losses occasioned by theft, fire, severe weather, injury to third parties, and the like, and may do so at trust expense.¹⁴⁸ Again, the entrusted property must be reasonably insured. Thus, when a particular risk of loss is slight and the cost to the trust estate of insuring against that risk excessive, the trustee, absent special facts, may elect not to insure against the risk and may well be duty-bound not to do so. Should the remote risk later materialize, the trust estate, not the trustee personally, bears the burden of the loss.¹⁴⁹ As to entrusted bank deposits, the reader is referred to the FDIC Guide to Calculating Deposit Insurance Coverage for Revocable and Irrevocable trusts.¹⁵⁰

Looking after entrusted real estate. Trust real estate should be routinely inspected, at least annually or more often as circumstances warrant, and appraised at least every three years. Property taxes should be paid in a timely fashion to avoid a tax sale.¹⁵¹ If the trust property is subject to a mortgage, the trustee must take reasonable steps to prevent a loss of the property due to foreclosure. The trustee should take all reasonable steps to ensure that no trust beneficiary is engaging in criminal activity, such as drug-dealing, on the entrusted premises; to do otherwise is to risk having the premises seized as contraband in a criminal forfeiture proceeding in derogation of the equitable property rights of the innocent beneficiaries.¹⁵²

A trustee may properly use trust funds to keep entrusted buildings and equipment in good repair.¹⁵³

Looking after entrusted insurance contracts. While it is true that a trustee generally has no duty to use personal funds to keep entrusted insurance contracts in force, he is nonetheless duty-

¹⁴⁶3 Scott & Ascher §18.1.2.6 (When Trustee Improperly Incurs Expense).

¹⁴⁷3 Scott & Ascher §18.1.2.6 (When Trustee Improperly Incurs Expense).

¹⁴⁸See Bogert §599; 3 Scott & Ascher §17.8 (noting that a trustee who has used reasonable care in the selection of an insurer will not be liable for a loss caused by the insurer's failure).

¹⁴⁹See, e.g., *Regions Bank v. Lowrey*, 101 So. 3d 210 (Ala. 2012) (trustee's failure to have insured an extensive tract of entrusted timberland against the hurricane damage that had befallen the tract held not a breach of trust).

¹⁵⁰<<http://www.fdic.gov/regulations/laws/federal/2008/08sep26rule.html>> (last accessed Aug. 18, 2017). See also <<http://www.cdars.com/?gclid=CIfDIqfI684CFQ8yaQod8RQP2A>> (last accessed Aug. 18, 2018) (The CDARS Program).

¹⁵¹See Bogert §602; 3 Scott & Ascher §17.8; 2A Scott on Trusts §176.

¹⁵²See, e.g., *3607 Tampico Dr. v. State*, No. 11-13-00306-CV, 2015 Tex. App. LEXIS 13056 (Tex. App. Dec. 31, 2015), *petition for review denied sub nom.* 0.089 Acres of Land Block 015, Lot 12 v. State, No. 16-0101, 2017 Tex. LEXIS 158 (Feb. 17, 2017).

¹⁵³3 Scott & Ascher §17.8 (noting that if the trustee's failure to keep a premises in good condition causes it to be "untenantable," the trustee may be liable for the loss of rentals).

bound to take reasonable steps to see to it that the premiums are either paid with entrusted funds or by someone else, such as a willing beneficiary of the trust. The typical trust instrument will contain exonerating boilerplate similar to the following: *The Trustee shall be under no obligation to pay the premiums which may become due and payable under the provisions of such policy of insurance, or to make certain that such premiums are paid by the Settlor or others, or to notify any persons of the nonpayment of such premiums, and the Trustee shall be under no responsibility or liability of any kind in the event such premiums are not paid as required.*

One thing is for sure: No matter how expansive and detailed the purported exoneration, if the trustee is on actual or constructive notice that an entrusted policy is about to lapse due to unintentional premium nonpayment, he is duty-bound to take reasonable steps to prevent the lapse, short of reaching into his own pocket.² “Perhaps the most fundamental aspect of acting for the benefit of the beneficiaries is protecting the trust property....[Such exonerating language]...cannot be relied upon to abrogate...[the Trustee’s]...duty to act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.”¹⁵⁴

If the risk to the trust estate is attributable to the trustee’s own negligence, say the trustee had undertaken to furnish the insurance company with an address to which notifications should be sent and the address had been wrong, then he could well be financially on the hook for any consequential economic harm to the trust estate.¹⁵⁵

The trustee should not compete with the trust. “While normally associated with corporations and with their directors and officers, what is usually referred to as the corporate opportunity doctrine also applies to...[trustees]...”¹⁵⁶ Accordingly, a beneficiary may void a transaction entered into by the trustee that involved an opportunity belonging to the trust, *e.g.*, the trustee’s entering into a business in direct competition with a business owned by the trust or purchasing an investment for himself that the facts suggest should have been purchased for the trust.¹⁵⁷

A trustee wishing to exploit an opportunity belonging to the trust or otherwise compete with the trust, of course, may do so notwithstanding the aforementioned proscriptions if the terms of the trust authorize it. Absent express authority in the governing instrument or some enabling statute, the trustee could attempt to obtain the informed consent of all beneficiaries, both current beneficiaries and remaindermen, or a court order. Either option, however, can be expensive if not problematic when there are unborn or unascertained beneficiaries in the picture. However the trustee attempts to get around the default law, the trustee has an internal overarching duty to act in good faith. This would include fully disclosing to the beneficiaries all information, both of a factual and legal nature, they would need to protect their equitable interests.

² See, *e.g.*, Matter of Wilkinson, 179 A.D.3d 817, 117 N.Y.S.3d 683 (2020).

¹⁵⁴Rafert v. Meyer, 859 N.W.2d 332 (Neb. 2015).

¹⁵⁵See, *e.g.*, Rafert v. Meyer, 859 N.W.2d 332 (Neb. 2015).

¹⁵⁶UTC §802 cmt.

¹⁵⁷UTC §802 cmt.

Legitimate claims against predecessor fiduciaries and cotrustees. A legitimate claim against a predecessor trustee or the settlor's estate (or personal representative) should be pursued on behalf of the trust.¹⁵⁸ A trustee who has reason to suspect that a cotrustee is depleting or about to deplete the trust property must take reasonable steps to prevent him from doing so.¹⁵⁹

Claims by and against third parties. A trustee shall take reasonable steps to enforce claims of the trust against third parties and, as we shall see, to defend claims against the trust by third parties.¹⁶⁰ (One court has even found that a trustee had a duty to enforce a claim against a contingent remainderman that predated the trust).¹⁶¹ Accordingly, the trustee has full power to sue on behalf of the trust estate and to defend suits that put the trust estate at risk.¹⁶²

One court has authorized a trustee to assign away *for adequate consideration* a trust claim against a third party.¹⁶³ The assignee was better equipped to prosecute the claim, the trust being cash-starved and no lawyer being found willing to take the matter on a contingent fee basis. The court found 55 percent of any recovery to be adequate consideration. This contractual right to a percentage of the recovery replaced the claim as a trust asset.

The trustee's duty to prudently litigate. Again, the trustee of a trust that is strapped for cash has no obligation to use his personal funds to underwrite remedial litigation¹⁶⁴ or litigation to collect insurance proceeds or other assets due the trust, unless the beneficiaries are willing to foot the bill with their own funds, although there may be an affirmative duty to solicit their voluntary indemnity.¹⁶⁵ "A trustee who can obtain the necessary funds by a sale or a mortgage of trust property may be under a duty to do so,"¹⁶⁶ provided it is reasonably likely that the costs of selling or encumbering the trust property is worth the benefits that could reasonably be expected to be obtained from the litigation. In any case, a trustee who is contemplating serious litigation at trust

¹⁵⁸See 3 Scott & Ascher §17.9; 2A Scott on Trusts. §177; Bogert §§592, 594.

¹⁵⁹See Restatement (Third) of Trusts §81 cmt. d.

¹⁶⁰UTC §811; Restatement (Third) of Trusts §76 cmt. d. See also 3 Scott & Ascher §§17.9 (Duty to Enforce Claims), 17.10 (Duty to Defend Actions); 2A Scott on Trusts §178; Bogert §581. Cf. §6.2.6 of this handbook (trustee's duty to defend the trust against attack, and certainly not to attack the trust).

¹⁶¹See, e.g., *New Haven Sav. Bank v. LaPlace*, 66 Conn. App. 1, 783 A.2d 1174 (2002) (noting that the defendant failed to cite any law holding that a trustee must forbear foreclosing a mortgage on a note held by the trust because the maker of the note is a contingent remainderman).

¹⁶²See Bogert §§594, 869; §6.2.6 of this handbook (trustee's duty to defend the trust against attack, and certainly not to attack the trust).

¹⁶³See *Dunmore v. Dunmore*, No. C063910, 2012 WL 267725 (Cal. Ct. App. Jan. 30, 2012) (unpublished).

¹⁶⁴Lewin ¶121-50 (England).

¹⁶⁵Restatement (Third) of Trusts §76 cmt. d. See generally Bogert §582; 3 Scott & Ascher §17.8; 2A Scott on Trusts §175.

¹⁶⁶3 Scott & Ascher §17.8.

expense would be well advised to seek a second legal opinion before proceeding.¹⁶⁷ He may even have a fiduciary duty to do so. Perhaps taking security for the claim in lieu of litigating it is a better option.¹⁶⁸ Or possibly putting the collection process on temporary hold would be a better way to go, provided there is a chance that doing so would increase the chances of a satisfactory resolution of the matter.¹⁶⁹ Likewise, a trustee has no duty to employ personal funds to fend off claims *against the trust estate*, unless the claims have been occasioned by some breach of trust.

As a general rule, all demands must be pressed, even to the extent of bringing suit,¹⁷⁰ or else the trustee will be liable for any loss caused by unjustified forbearance.¹⁷¹ Take, for example, the trustee who holds legal title to contractual rights against a third party, such as rights against the corporate issuer of a bond or rights against an insurance company incident to an insurance policy. The third party, instead of making a payment to the trustee, who is the other party to the contract, takes it upon itself to make a payment directly to a trust beneficiary who is not of full age and legal capacity. The trustee may have a fiduciary duty to seek to compel the third party to make the payment a second time, this time to the trustee.¹⁷²

A trustee who is unsuccessful at the trial level in pressing a claim may have a duty to appeal the decision to a higher court, provided it would be reasonable and in the interests of the

¹⁶⁷See also §8.25 of this handbook (noting that trustees can no longer assume that every lawyer has been exposed in an academic setting, or anywhere for that matter, to the fundamentals of agency and trust law).

¹⁶⁸See generally 3 Scott & Ascher §17.9 (noting that “it may be reasonable for the trustee to take security for the claim, even if doing so would not otherwise be part of a prudent investment strategy for the trust”).

¹⁶⁹See generally 3 Scott & Ascher §17.9.

¹⁷⁰See 3 Scott & Ascher §17.9; 2A Scott on Trusts §177; UTC §812. See, e.g., *PriceWaterhouseCoopers, LLP v. Bassett*, 666 S.E.2d 721 (Ga. Ct. App. 2008) (trustees of interests in a now bankrupt business enterprise successfully brought suit against its corporate accountants for negligently misrepresenting the financial condition of the enterprise, a misrepresentation that had induced the trustees to acquire the interests for various family trusts).

¹⁷¹See 3 Scott & Ascher §17.9; 2A Scott on Trusts §177; UTC §812.

¹⁷²The third-party obligor who makes a payment directly to the trust beneficiary instead of to the title-holding trustee, the other party to the contract, does so at his, her, or its peril, unless directed to do so by the trustee. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). If the beneficiary is not of full age and legal capacity, the third party obligor runs the risk of having to pay twice. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). There is a similar risk if following the direction were to constitute a knowing participation with the trustee in a breach of trust or if the trust were a spendthrift trust. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person).

beneficiaries to do so.¹⁷³ “The trustee is not excused from enforcing a claim merely because the settlor would not have pressed it or because of generous feelings for the obligor.”¹⁷⁴ On the other hand, it may be in the economic interest of the beneficiaries, and therefore prudent and reasonable, to forbear or to compromise a claim or submit it to arbitration.¹⁷⁵ Because of the attendant expense to the trust, the patently futile prosecution of a claim itself can constitute a breach of the specific duty to protect the trust property.¹⁷⁶ State statutes authorize a trustee to compromise, usually with court approval.¹⁷⁷

Imprudently compromising claims by and against the trust estate. In the absence of express authority in the governing instrument to do so, the trustee inclined to compromise a claim should check for an applicable statute. If one is found, its provisions should be followed. In the absence of such a statute, the trustee has two options: to obtain the consent of the current beneficiaries and remaindermen, if feasible, or to seek court approval. Note: If the claim is *de minimis*, taking such precautions would not be commensurate with the trustee’s potential liability and thus could constitute a breach of the trustee’s duty of loyalty, and ironically his duty not to waste the trust property.

Ordinarily, the trustee has a duty to defend third-party actions that might result in a loss to the trust estate, and to appeal adverse decisions to the extent it is reasonable and in the interest of the beneficiaries to do so.¹⁷⁸ “It might also be reasonable to settle an action or suffer a default rather than to defend an action.”¹⁷⁹ Consuming trust property in a patently futile defense of a claim against the trust estate can itself constitute a breach of trust. At minimum, the trustee risks personal liability for the defense costs.¹⁸⁰

Administering provisions that are unlawful or violate public policy. Likewise, notwithstanding the duty to carry out the terms of his trust,¹⁸¹ there is a countervailing duty on the

¹⁷³See generally 3 Scott & Ascher §17.9 (noting that the trustee generally has “wide discretion” whether or not to appeal and risks being second-guessed only when there has been an abuse of that discretion).

¹⁷⁴3 Scott & Ascher §17.9 (noting that “[t]he trustee may not be generous, at the beneficiaries’ expense”).

¹⁷⁵See Restatement (Third) of Trusts §76 cmt. d; Restatement (Second) of Trusts §192; 3 Scott & Ascher §17.9.

¹⁷⁶See Restatement (Second) of Trusts §192 cmt. c; 3 Scott on Trusts §192; §6.2.6 of this handbook (the trustee’s duty to defend the trust against attack, and certainly not to mount an attack against the trust).

¹⁷⁷See 3 Scott on Trusts §192.

¹⁷⁸See generally 3 Scott & Ascher §17.10.

¹⁷⁹UTC §811 cmt. See generally 3 Scott & Ascher §17.10.

¹⁸⁰See, e.g., *In re Beddoe* (Downes v. Chatham), [1893] 1 Ch. 547 (Eng.).

¹⁸¹See §6.1.2 of this handbook (the trustee’s duty to affirmatively carry out the terms of the trust).

part of the trustee, a duty that runs to the beneficiaries, not to carry out provisions that are unlawful or violate public policy.¹⁸² The trustee also has a duty not to attempt to comply with a provision if compliance would be impossible or incur unreasonable expense.¹⁸³

Appendix B

§5.4.1.8 Right and Standing of Beneficiary to Proceed in Stead of Trustee Against Those with Whom the Trustee Has Contracted, Against Tortfeasors, and Against the Trustee's Agents, *i.e.*, Against Third Parties [from *Loring and Rounds: A Trustee's Handbook* (2021)].

*In the old law of uses, it was held that where the feoffee to uses was disseised by a third person the cestui que use could not maintain a suit in equity against the third person even though he had notice of the use.*¹¹⁴

*In the present situation, it is clear from the complaint the beneficiary could prove facts showing she had standing to bring suit against the third parties for the improper distribution of stock. She could show, at the very least, the trustee improperly neglected to bring action against the appellees when he waited over ten years after the improper transfer and still did not bring suit.*¹¹⁵

Standing and procedure. The trustee is the one primarily responsible for seeing to it that harm done to the trust by a third party, such as an investment advisor, is remedied.¹¹⁶ This is an affirmative duty. If the trustee fails to take suitable action, then the beneficiary may step into the shoes of the trustee and deal directly with the third party.¹¹⁷ The trustee's forbearance, however, must be improper or wrongful.¹¹⁸ As we make clear in §6.2.1.3 of this handbook, the failure of a

¹⁸²Restatement (Third) of Trusts §72. See generally §6.2.12 of this handbook (the trustee's duty not to comply with provisions that are unlawful or violate public policy).

¹⁸³Restatement (Third) of Trusts §73. See generally §6.2.13 of this handbook (the trustee's duty not to attempt to comply with a trust provision if compliance would be impossible or incur unreasonable expense).

¹¹⁴4 Scott on Trusts §282 (citing to Chudleigh's Case, 1 Eng. Rep. 114, 139b (1589–1595)). See generally §8.15.1 of this handbook (statute of uses).

¹¹⁵Anderson v. Dean Witter Reynolds, Inc., 841 P.2d 742, 745 (Utah 1992) (citing with approval Restatement (Second) of Trusts §282, which in part provides that if a trustee improperly refuses or neglects to bring an action against a third person, the beneficiary can maintain a suit in equity against the third person).

¹¹⁶See generally 5 Scott & Ascher §28.1.

¹¹⁷4 Scott on Trusts §§282, 282.1; Restatement (Second) of Trusts §§281–282; 5 Scott & Ascher §28.2.1.

¹¹⁸See *In re XTO Energy, Inc.*, 471 S.W.3d 126 (Tex. App. 2015).

trustee to enforce a claim against a third party is not *per se* a breach of trust.

The beneficiary might bring an equitable derivative suit on behalf of the trust against the third party when all else fails.¹¹⁹ To memorialize the trustee's improper/wrongful inaction, the beneficiary will want to make a formal written demand upon the trustee before taking matters into his or her own hands. The court may award the beneficiary litigation costs if the litigation is deemed beneficial to the trust.¹²⁰ Any common law causes of action would be based on one or more of the following: breach of contract (contract); tortious conduct (tort); and breach of fiduciary duty (agency).¹²¹ Analogous derivative doctrine prevails in the wills context: “Although court-appointed fiduciary managers in probate proceedings have broad statutory authority to bring all actions necessary to collect assets, preserve and protect the estate,...nothing in that body of law expressly prohibits a court from granting a beneficiary leave to bring an action on behalf of the estate when there are special circumstances that take the case out of the general rule.”¹²²

The Restatement (Third) of Trusts provides that a trust beneficiary may maintain a proceeding related to the trust or its property against a third party only if the beneficiary is in possession, or entitled to immediate distribution, of the trust property involved; *or* if the trustee is “unable, unavailable, unsuitable or improperly failing to protect the beneficiary’s interest.”¹²³ There is an admonition that accompanies the authorization: “It bears repeating that the trustee, and not a beneficiary, is ordinarily the only proper person to bring (and to decide whether to bring) an action on behalf of the trust against a third party.”¹²⁴

The UPC would grant the beneficiary standing to petition the court directly, *i.e.*, without having first made a demand upon the trustee, to “review the propriety of employment of any person by a trustee including any attorney, auditor, investment advisor or other specialized agent or assistant, and the reasonableness of the compensation of any person so employed....”¹²⁵

In the case of a trustee mutual fund, before an investor-beneficiary may bring a derivative suit on behalf of the fund against, say, the third-party fund sponsor, it is likely that the investor-beneficiary must first make a formal demand upon the trustees to take suitable action.¹²⁶ This is an example of the statutory law of corporations encroaching back upon the law of trusts. “Likewise,

¹¹⁹See UTC §1004 cmt.; Lewin ¶43-05 (England); 5 Scott & Ascher §28.2.1 (U.S.).

¹²⁰3 Scott on Trusts §188.4; UTC §1004 cmt.

¹²¹See *generally* 5 Scott & Ascher §28.2.1 (When the Trustee Fails to Sue).

¹²²Estate of Bleeker v. Arvest Trust Co., 2007 OK 68, 168 P.3d 774 (Okla. 2007).

¹²³Restatement (Third) of Trusts §107(2).

¹²⁴Restatement (Third) of Trusts §107 cmt. c(2).

¹²⁵UPC §7-205. “Any person who has received excessive compensation from a trust may be ordered to make appropriate refunds.” UPC §7-205.

¹²⁶ING Principal Prot. Funds Derivative Litig., 369 F. Supp. 2d 163, 170–171 (D. Mass. 2005) (suggesting that the prederivative litigation universal demand requirement is applicable to business trusts such as trustee mutual funds, as well as to corporations).

when property is conveyed by deed of trust to...[an indenture trustee]...to secure an issue of bonds, and the trustee, upon default, refuses to bring a proceeding for foreclosure, one or more of the bondholders can maintain a suit for foreclosure, joining the trustee and obligor as defendants.”¹²⁷

For more on the inbound external liabilities of third parties to the trustee or the beneficiary, or both, see §3.6 of this handbook.

Contract and tort. For a successful breach of contract action to lie against the third party, the beneficiary would have to prove that the trustee had entered into a contract for goods or services with the third party on behalf of the trust, that the third party had breached the contract, and that the beneficiary's equitable interest had been harmed as a result thereof.

For a successful tort action to lie, the beneficiary would have to prove that the third party had committed some tort that had adversely affected in some way the beneficiary's equitable interests, *e.g.*, trespassing on trust land.¹²⁸ Should the beneficiary successfully prove the third party's knowing participation in a breach of trust, many of the remedies that are available as against the trustee would be available as well as against the third party (in fact, their liability would be joint and several).¹²⁹ “Thus, if the trustee directs an agent to sell trust property, which the agent knows the trustee is not authorized to sell, and he does sell it, he is liable for participation in the breach of trust.”¹³⁰ If the agent takes title to the property, he becomes an involuntary trustee, technically a constructive trustee, of the property.¹³¹

Agency. If a third party is acting as an agent of the trustee for purposes of assisting the trustee in carrying out his fiduciary responsibilities, there are three possibilities, assuming the third party has *not* been knowingly facilitating and participating in any breaches of trust by the trustee: The third party could have fiduciary duties that ran to the trustee alone, to the beneficiary alone, or to both.¹³²

If the agent has fiduciary duties that ran to the beneficiary alone, an unlikely if not illogical scenario, the beneficiary would have standing to bring an action against the third party for any breach of fiduciary duty to the beneficiary.

If the agent has fiduciary duties that ran to the trustee alone, the beneficiary would have no

¹²⁷5 Scott & Ascher §28.2.1. *See generally* §9.31 of this handbook (corporate trusts; trusts to secure creditors; the trust indenture act of 1939; protecting bondholders).

¹²⁸Scott on Trusts §§280.2, 280.3.

¹²⁹Bogert §868. *See also* 5 Scott & Ascher §28.2.

¹³⁰Restatement (Second) of Trusts §326 cmt. a.

¹³¹Scott on Trusts §288; 5 Scott & Ascher §28.2. *See generally* §3.3 of this handbook (involuntary trustees) (discussing the constructive trust).

¹³²With respect to the trustee's legal counsel, *see* *Chinello v. Nixon, Hargrave, Devans & Doyle*, 788 N.Y.S.2d 750 (2005) (confirming that in New York, absent fraud, collusion, malicious acts, or other special circumstances, counsel to the trustee is not liable to third parties not in privity, *e.g.*, the beneficiaries of the trust, for harm caused by counsel's professional negligence).

standing to go against the agent. Some courts, for example, have held that trust counsel is such an agent.¹³³ Other courts have granted beneficiaries standing, holding that trust counsel has some duties that run to the beneficiary as well as to the trustee.¹³⁴

If the agent has fiduciary duties that run to both the trustee and the beneficiary, presumably each would have standing to sue the agent. What if a trust officer, an agent of his or her corporate employer, knowingly causes the employer to commit a breach of trust? Would the beneficiary, as well as the trustee-employer, have standing to sue the trust officer and could the trust officer be found personally liable? The answer is likely to be yes on both counts.¹³⁵ “The question is of great importance to the beneficiaries if the bank is insolvent.”¹³⁶ The Uniform Prudent Investor Act provides that an agent in performing a delegated function owes a duty *to the trust* to exercise reasonable care to comply with the terms of the delegation.¹³⁷ One can reasonably assume that one consequence of an agent having duties that run *to the trust* is that the trustee and the beneficiary each would have standing to sue the agent.

¹³³See generally §8.8 of this handbook (whom trust counsel represents); 4 Scott on Trusts §326.4.

¹³⁴See generally §8.8 of this handbook (whom trust counsel represents); 4 Scott on Trusts §326.4.

¹³⁵See generally §7.2.9 of this handbook (personal liability of the trustee's agents and other third parties to the beneficiary); 4 Scott on Trusts §326.3.

¹³⁶Scott on Trusts §326.3 at 303.

¹³⁷Unif. Prudent Investor Act §9(b).