Title

Is a trust term directing that internal trustee-beneficiary fiduciary disputes be arbitrated judicially enforceable?

Text

A recent narrowly focused decision of the Supreme Court of Virginia holds that a trust term directing that trustee-beneficiary disputes be arbitrated is unenforceable. See Boyle v. Anderson, 871 S.E.2d 226 (Virginia 2022). Reasoning? Virginia's Uniform Arbitration Act and the Federal Arbitration Act provide for enforcement of arbitration clauses in contracts, whereas a trust, *qua* trust, is not a contract. A trust is *sui generis* in that a trust beneficiary, *qua* beneficiary, assumes no duties, fiduciary, or otherwise. Beneficiaries of a trust generally do not provide any consideration to the settlor of a trust. That a successor trustee was not around at the trust's inception would not render the trust itself unenforceable upon his assumption of office. Many an enforceable trust will have yet-to-be-conceived and/or currently unascertainable beneficiaries. One could go on and on. While a trust *may be established* incident to contract, no way is a trust, *qua* trust, a contract. But there also is non-statutory background equity doctrine which, as a practical matter, militates against the enforceability of arbitration clauses in the trust context, even in the few jurisdictions whose arbitration statutes proport to provide for enforcement of arbitration clauses in trust instruments as well as in written contracts.

If a particular *internal* trust dispute is resolvable by agreement among all interested parties, including the trustee, then it should follow that the parties are entitled to submit the dispute to nonjudicial binding arbitration. But not all trust disputes necessarily are, such as those that turn on technical construction of trust deeds or wills, cases in which injunctions are sought and claims involving allegations of fraud. So also some trust disputes, on public policy grounds, may not be arbitrable in a nonjudicial context, such as a dispute over the validity of a testamentary trust or whether there has been a violation of the rule against perpetuities. Likewise, a contest over the *validity* of an inter vivos trust, or the *validity* of a purported amendment to it, remains the exclusive domain of the judiciary, no matter what the contested documentation may have to say on the subject of arbitration. As a general matter, a trust term that purports to oust the court of its traditional equitable jurisdiction over trust matters has always been considered unenforceable, such as one that purports to bestow on a member of the executive branch of a state's government the authority to make binding determinations as to whether the trustee is complying with the other trust terms. Nor has it been considered possible to oust the court by an expansive grant of discretion to the trustee. "It is submitted…that, even as to matters thus firmly committed to the trustee's discretion, judicial review should remain available if the trustee acts in bad faith, contrary to the terms of the trust, or with an improper motive." 3 Scott & Ascher §18.2

In any case, assuming a particular trust dispute may be fully arbitrated nonjudicially, for the process to work, that is for the arbitrator's decisions to be final and binding on all persons, each interested party will need to be represented by independent counsel, or give an informed waiver of counsel, unless the trust is revocable, which is a whole other matter. As the typical donative/noncommercial trust will have unborn and unascertained beneficiaries requiring the services of a court-appointed guardian ad litem, absent very special facts, it is hard to see how the court can be kept altogether out of the process. If some of the current beneficiaries are minors, then the court almost certainly will have to be involved. Thus, whether arbitration is an option worth pursuing when there are unborn and/or unascertained beneficiaries (or minor beneficiaries) will depend upon whether its attendant redundancies and inefficiencies are outweighed by its advantages.

As to whether an arbitration clause in a contract between a trustee and his third-party investment agent may bind the trust's beneficiaries, see §6.1.4 of *Loring and Rounds: A Trustee's Handbook* (2022). The relevant parts of the section are reproduced in the appendix immediately below. The 2022 Edition of the Handbook is available for purchase at https://law-store.wolterskluwer.com/s/product/loring-rounds-a-trustees-handbook-2022e-misb/01t4R00000OVWE4QAP.

Appendix

§6.1.4 *Trustee's Duty to Give Personal Attention (Not to Delegate)* [from *Loring and Rounds: A Trustee's Handbook* (2022), available for purchase at: https://law-store.wolterskluwer.com/s/product/loring-rounds-a-trustees-handbook-2022e-misb/01t4R00000OVWE4QAP.

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The pre-dispute arbitration contract between a trustee and his investment agent (IA): Are the trust beneficiaries bound? While the trustee is the principal and a third party (the IA) is the agent, the intersection of agency doctrine and trust doctrine can complicate matters. Assume that the agency services being rendered on behalf of the trust involve the performance of certain fiduciary functions that require the exercise of discretion and that some of the trust beneficiaries are unborn or currently unascertainable remaindermen. As they are neither parties to the agency nor parties to the arbitration contract incident to it, it is hard to see how at least *they* (the beneficiaries) can be bound by the arbitration contract in a dispute between them and the IA.[646] Even more so if, say, the IA has participated with the trustee in a breach of trust. Moreover, pursuant to statute—specifically §807(b) & (c), taken together, of the UTC and §9(b) & (c), taken together, of the Uniform Prudent Investor Act (UPIA)—fiduciary duties run from the IA directly to the beneficiaries incident to the trustee's general delegation of discretionary authority, not incident to the terms of the particular trustee-IA agency agreement. For the terms of the incidental arbitration contract to be binding on the unborn and currently unascertainable, it would seem that a guardian ad litem judicially charged with representing their interests would have to have been a party to the contract at the time it was entered into. Recall that under classic trust doctrine, the trustee, *qua* trustee, is not the beneficiaries' agent.[647] In other words, a trust is not an agency. For authority for the proposition, see generally §9.9.2 of this handbook.

As a side note, the sections of the UTC and UPIA cited immediately above do not appear to hold the amateur agent-fiduciary to a lower fiduciary standard of conduct than the professional agent-fiduciary. The UTC (specifically §806) and the UPIA (specifically §2(f)), on the other hand, expressly hold the professional *trustee* to a higher fiduciary standard of conduct than the amateur *trustee*.

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[646] *See generally* Charles E. Rounds, Jr., *Arbitration Contracts Between Trustees and Their Investment Agents: A Warning Label*, 93 N.D. L. Rev. 263 (2018).

[647] *See generally* §5.6 of this handbook.