Texas Fiduciary Litigation Update 2018-2019

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Introduction

- Fiduciary litigation is an ever changing area of the law.
- The author reviews and reports on new cases regularly at his blog: Texas Fiduciary Litigator (www.txfiduciarylitigator.com)
- “The Intersection of Texas Courts and The Fiduciary Field.”
- You can sign up for email alerts!
- This presentation is intended to provide an update on current legal precedent that impacts fiduciaries.

Merger Of Trusts

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Merger Of Trusts

- In *In re Macy Lynne Quintanilla Trust*, a settlor created three trusts for his children in 2014. No. 04-17-00753-CV, 2018 Tex. App. LEXIS 8223 (Tex. App.—San Antonio October 10, 2018, no pet.).
- After the settlor and the trust protector had a falling out, the settlor created three new trusts in 2016.
- The 2016 trusts were virtually identical to the 2014 trusts, except that they named a new trust protector.
- The trustee then executed three agreements to merge each of the 2014 trusts into the 2016 trusts.

Merger Of Trusts

- Trust protector argued that the new trusts were not proven to be properly funded.
- The court of appeals held that “a trust agreement itself may be sufficient summary judgment evidence that the trust was in fact funded. Absent any evidence in the record to the contrary, we conclude Perry met his summary judgment burden of demonstrating no genuine issue of material fact exists that the 2016 Trusts were funded.” *Id*.
- The trust protector also argued that the trustee did not conclusively establish that the trusts were properly merged.
- The court of appeals disagreed and cited to the 2014 trust agreements that allowed them to be merged and the merger agreements stated that the trustee had determined that the merger would not impair the rights of any beneficiary or adversely affect achievement of the purposes of the trusts.

Merger Of Trusts

- The court held that there was scant authority interpreting when a merger “impair[s] the rights of any beneficiary or adversely affect[s] achievement of the purposes of one of the respective trusts.”
- The trust protector argued that the merger adversely affected the purpose of the 2014 trusts because it removed him.
- The court disagreed: “the 2014 trust agreements do not provide a method for removing or replacing the Trust Protector that was circumvented by merging the trusts.”
- The court held that under the trusts and the statute the trustee did not have to provide the trust protector notice, only the beneficiaries.
- Finally, the court held that the trust protector did not have standing because he was not an interested party: “generally, a person who does not manage a trust (a trustee) or stand to inherit any trust assets (a beneficiary) is not an ‘interested person’ by virtue of being a ‘person who is affected by the administration of the trust.’”

Trust Failure

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Trust Failure

- In *In re Estate of Moore*, a decedent executed a will that provided that the residuary of his estate would be held in trust for his mother, and such trust would terminate on her death with the assets then passing to certain charitable remainder beneficiaries. No. 05-18-00019-CV, 2019 Tex. App. LEXIS 3871 (Tex. App.—Dallas May 14, 2019, no pet. history).
- The decedent's mother predeceased him.
- The decedent's sole heir then alleged that the trust failed because the sole beneficiary predeceased the decedent and that she should receive the assets.

Trust Failure

- The heir challenged the trial court's construction, arguing : (1) there were no living beneficiaries of the trust at the time of the decedent's death; and (2) the trust's creation was made expressly contingent on the decedent's mother surviving him.
- Court held that the term beneficiary included remainder beneficiaries: "even though the trust's life beneficiary (Moore's mother) was no longer living at the time the conveyance became operative, there were other named remainder beneficiaries sufficient to prevent the trust from failing."

Trust Failure

- Regarding the heir's second argument, the will provided: "My residuary estate shall pass and vest in the Trustee hereinafter named, IN TRUST, in the following manner..."
- "This statement is not qualified by a condition precedent; rather, it is the subsequent statement creating Moore's mother's interest in the trust that is qualified by a condition precedent: 'My residuary estate shall be held as a trust for the benefit of my mother, . . . if she is surviving at the time of my death[.]'"
- The court held that because Moore's mother did not survive him, the condition precedent to her interest was not satisfied, her interest terminated, and the remainder interests "either became present interests or became closer to present interests."

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Reformation Of A Trust

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Reformation Of A Trust

- In 2017, the Texas Trust Code was amended to provide that on the petition of a trustee or a beneficiary, a court may order that the terms of the trust be reformed if: (1) reformation of administrative, nondispositive terms of the trust is necessary or appropriate to prevent waste or impairment of the trust's administration; (2) reformation is necessary or appropriate to achieve the settlor's tax objectives or to qualify a distributee for governmental benefits and is not contrary to the settlor's intentions; or (3) reformation is necessary to correct a scrivener's error in the governing document, even if unambiguous, to conform the terms to the settlor's intent. Tex. Prop. Code §112.054(b).
- Subsections (e) and (f) also provide: "(e) An order described by Subsection (b-1)(3) may be issued only if the settlor's intent is established by clear and convincing evidence."
- "(f) Subsection (b-1) is not intended to state the exclusive basis for reformation of trusts, and the bases for reformation of trusts in equity or common law are not affected by this section."

Reformation Of A Trust

- In *In re Ignacio G. & Myra A. Gonzales Trust*, a couple formed a trust and named their daughter as the trustee. No. 06-19-00014-CV, 2019 Tex. App. LEXIS 4648 (Tex. App.—Texarkana June 6, 2019, no pet. history).
- The trust identified the settlors' children as the two children that they had together.
- However, the trust then used the undefined term "descendants" in discussing beneficiaries.
- The trustee/child filed suit to reform the trust to clarify that an older child of the mother was not a beneficiary.

Reformation Of A Trust

- The court noted that Section 112.054 of the Texas Property Code provides that a court may order the terms of a trust modified if "reformation is necessary to correct a scrivener's error in the governing document, even if unambiguous, to conform the terms to the settlor's intent" and such intent is established by clear and convincing evidence. *Id*. (citing Tex. Prop. Code Ann. § 112.054(b-1)(3), (e)).
- That provision was not effective at the time the trust was created, but the court noted that this provision was grounded in common law and the Restatement (Third) of Trusts and Restatement (Third) of Property.

Reformation Of A Trust

- "Reformation requires two elements: (1) an original agreement and (2) a mutual mistake made after the original agreement in reducing the original agreement to writing."
- "A court is without power to make a contract that the parties did not make; an actual agreement reached prior to the drafting of the instrument involved is a requisite to an action for reformation."
- "The mistake may be shown by parol evidence."
- "[A]lthough a mutual mistake of the parties is required in most instances, if a settlor of a trust receives no consideration for the creation of the trust, a unilateral mistake . . . is sufficient."
- "Any mistake of the scrivener which could defeat the true intention may be corrected in equity by reformation, whether the mistake is one of fact or law."

Reformation Of A Trust

- The court held that the trust clearly contained scrivener's errors.
- “[I]t is quite possible that the scrivener's error occurred in the identification article and should have included Edna.”
- “The identification article stated Ignacio and Myra only had two children. This was a scrivener's mistake of fact.”
- It is undisputed that Edna is Myra's natural child and that she was adopted by Ignacio.
- Court reversed summary judgment and found that a fact issue existed as to whether Edna was intended to be omitted as a beneficiary.

Reformation Of A Will

- Historically “In construing a will, the court’s focus is on the testatrix’s intent. This intent must be ascertained from the language found within the four corners of the will. The court should focus not on “what the testatrix intended to write, but the meaning of the words she actually used.” In this light, courts must not redraft wills to vary or add provisions “under the guise of construction of the language of the will” to reach a presumed intent. Determining a testatrix’s intent from the four corners of a will requires a careful examination of the words used. If the will is unambiguous, a court should not go beyond specific terms in search of the testatrix’s intent.”

Reformation Of A Will

- In 2015, the Texas Legislature now allows a court to look at extrinsic evidence to modify an unambiguous will upon certain circumstances. Tex. Est. Code § 255.451.
- The Texas Estates Code allows a personal representative to petition a court to modify or reform a will "if: (1) modification of administrative, nondispositive terms of the will is necessary or appropriate to prevent waste or impairment of the estate's administration; (2) the order is necessary or appropriate to achieve the testator's tax objectives or to qualify a distributee for government benefits and is not contrary to the testator's intent; or (3) the order is necessary to correct a scrivener's error in the terms of the will, even if unambiguous, to conform with the testator's intent."

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Reformation Of A Will

- Testator's intent must be established by clear and convincing evidence.
- Only a personal representative can bring a claim to modify a will.
- The trial court can reform a will so that it has retroactive effect.
- The statute provides for a protection for a personal representative who does not act to modify or reform a will.

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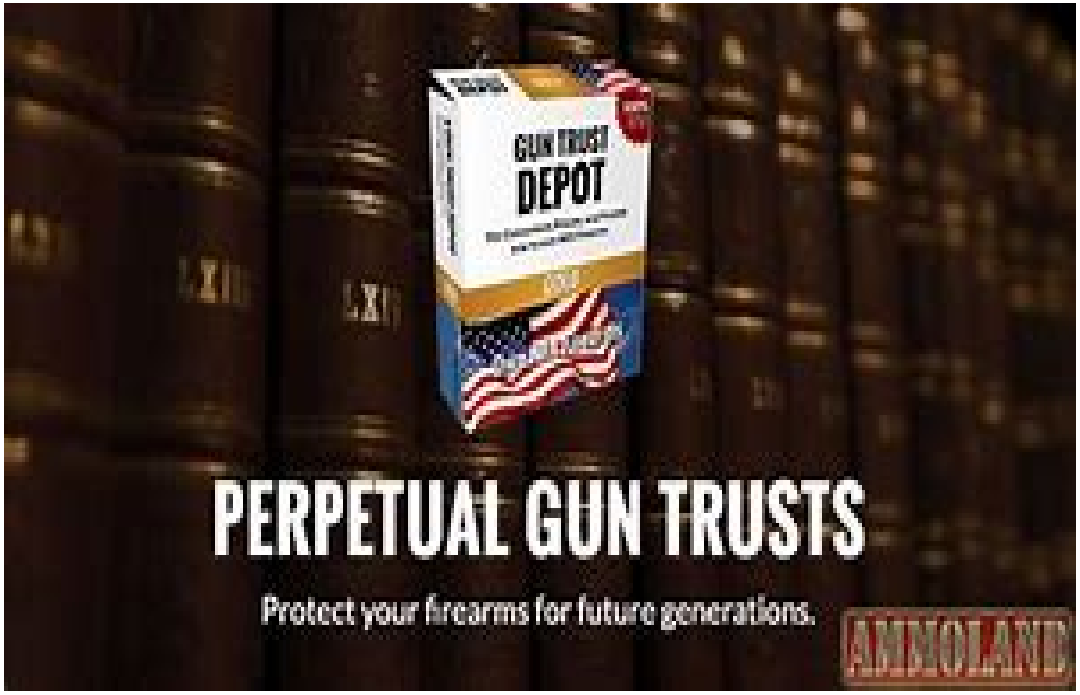
Gun Trusts


GUN TRUST
DEPOT
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AMMOLAND

Gun Trusts

- In *Estate of Keener*, two heirs of a settlor of a "gun" trust filed an application to declare heirship to his property. No. 13-18-00007-CV, 2019 Tex. App. LEXIS 1222 (Tex. App.—Corpus Christi February 21, 2019, no pet.).
- The beneficiary of the trust filed a plea in intervention in the heirship proceeding, arguing that the trust owned the property.
- The trial court denied his intervention, and the trust beneficiary filed an appeal of that order.

Gun Trusts

- The attorney advertised his gun trusts as vehicles used to easily transfer federally regulated firearms upon death and also as a way to legally share the use of a federally regulated category III asset, such as a silencer or suppressor, among multiple individuals.
- However, the terms of the trusts did not limit it to only firearms.
- The heirs argued that the trust was not intended to transfer anything more than the suppressor.
- The court of appeals disagreed and held that the beneficiary was an interested person under the Texas Estate's Code and was the owner of any property that was placed in the trust.
- "In other words, he has a claim against the property in Keener's estate that appellees seek to inherit."
- The court found that there was a fact issue as to the overall property in the trust and whether Schedule A added any property to the trust.

Statute Of Limitations

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Statute Of Limitations

- Fiduciaries are often in the position of a lender: a trustee may make a loan to a beneficiary.
- Sometimes the trustee has to collect on that debt when the borrower defaults, and that fight can revolve around the statute of limitations.
- Indeed, a trustee never wants to sue its beneficiary for any reason, and delay is often present in these circumstances.

Statute of Limitations

- In *Godoy v. Wells Fargo Bank, N.A.*, a bank sued a guarantor to recover on a deficiency following a foreclosure sale. No. 18-0071, 2019 Tex. LEXIS 443 (Tex. May 10, 2019).
- The defendant guarantor alleged that any such claim was barred by the two-year statute of limitations, and the lender argued that the guarantor waived the defense by provisions in the loan documents.
- Texas Supreme Court held: “Blanket pre-dispute waivers of all statutes of limitation are unenforceable, but waivers of a particular limitations period for a defined and reasonable amount of time may be enforced.”
- The Court held that the clause was sufficiently specific, was for a reasonable time, and ruled for the lender.

Statute of Limitations

- The *Godoy* opinion arms a trustee with one more tool.
- A trustee can have the note, guaranty agreement, or other similar document expressly state that the borrower waives the defense of the statute of limitations for a certain period of time (negotiated notes have a six year statute of limitations in Texas, and potentially, a waiver clause could extend that to eight years).

Statute Of Limitations

- In *Gilmore v. Rotan*, a testamentary trust's beneficiaries sued the trustees in 2015 for making a transfer of trust property in 2003 that was evidenced by a deed filed in 2010. No. 11-16-00253-CV, 2018 Tex. App. LEXIS 7705 (Tex. App.—Eastland September 20, 2018, no pet.).
- The court held that "Persons interested in an estate admitted to probate are charged with notice of the contents of the probate records."
- "Appellants had constructive notice of their beneficial interest in the real property when Harry Dean Rotan's will was admitted to probate. Constructive notice creates an irrebuttable presumption of actual notice. Accordingly, the summary judgment evidence establishes that Appellants had notice of their alleged injury in 2010. Since the applicable statute of limitations is four years for a claim for breach of fiduciary duty, Appellants' suit filed in 2015 was not timely."

Statute of Limitations

- In *Agar Corp. v. Electro Circuits Int'l,* the plaintiff asserted claims for tortious interference, breach of fiduciary duty, aiding and abetting breach of fiduciary duty, fraud, fraud by non-disclosure, misappropriation of trade secrets, violations of the Texas Theft Liability Act, conversion, and civil conspiracy. No 17-0630, 2019 Tex. LEXIS 351 (Tex. April 5, 2019).
- The defendant alleged that the conspiracy claim was barred by the two-year statute of limitations, and the court of appeals agreed with that argument.
- The Texas Supreme Court decided that limitations for a conspiracy claim is the same as the underlying tort.
- The Court reversed the summary judgment for the defendant and remanded because some of the plaintiff's conspiracy claims were derivative of claims that had a four-year limitations period and were not barred.

Supersedeas Bond

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Supersedeas Bond

- In *Wheatley v. Farley*, a trial court entered an order awarding relief to both parties, and both parties appealed. No. 08-18-00106-CV, 2019 Tex. App. LEXIS 4626 (Tex. App.—El Paso June 5, 2019, no pet. history).
- One party was a dependent administrator, and the trial court ruled that he did not have to post a supersedeas bond to stay execution of the judgment.
- Texas Estates Code Section 351.002 provides that an appeal bond is not required if an appeal is taken by an executor or administrator, unless the appeal personally concerns the executor or administrator.
- Even though an "appeal" bond is different from a supersedeas bond, the court of appeals held that "when an executor or administrator of an estate appeals, he or she is not required to post a supersedeas bond unless the appeal personally concerns the executor or administrator."

Diversity Of Citizenship

Diversity Of Citizenship

- In *Thunder Patch II, LLC v. JPMorgan Chase Bank, N.A.*, plaintiffs filed suit against a trustee in state court seeking a declaration regarding the enforceability of a mineral lease, and the trustee removed the case to federal court based on diversity of citizenship. No. 5-18-CV-00629-OLG-RBF, 2018 U.S. Dist. LEXIS 207696 (W.D. Tex. December 10, 2018).
- The court held that when a trustee is sued in its capacity as a trustee, it is the citizenship of the trustee—not the trust's beneficiaries—that matters for diversity of citizenship purposes.
- "This rule governs so long as the trustee has 'real and substantial control' over the trust's assets."
- Court held it had jurisdiction and denied motion to remand.
- Due to a national bank's ability to remove, many plaintiffs are adding bank employees as defendants to defeat complete diversity and diversity jurisdiction.

Trustee Liability

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Trust Disputes In Divorces

- In *In the Interest of K.K.W.*, an ex-wife sued an ex-husband and the trustee of a trust that they created for breaches of fiduciary duty and sought to remove the trustee, among other claims, arising out of the trustee's alleged unfair distribution of trust assets. No. 05-16-00795-CV, 2018 Tex. App. LEXIS 6539 (Tex. App.—Dallas August 20, 2018, pet. denied).
- Trial court granted summary judgment for defendants, which was largely affirmed.
- The court of appeals, however, reversed on a standing ground and held that wife had standing as an interested person as a remote contingent remainder beneficiary and also reversed on a removal claim because standing was the only ground asserted to defeat it.
- The court of appeals reversed a constructive fraud claim based on the alleged failure of the trustee to disclose a side-agreement with the husband because a "trustee owes the same fiduciary duty to a contingent beneficiary as to one with a vested interest."
- Attorney's fees award for defendants was affirmed.

Trust Dispute For Failed Investments

- In *Goughnour v. Patterson*, a beneficiary sued a trustee based on a failed real estate investment. No. 12-17-00234-CV, 2019 Tex. App. LEXIS 1665 (Tex. App.—Tyler March 5, 2019, pet. filed).
- In 2007, the trustee of four trusts invited his mother, the primary beneficiary, and his siblings, also beneficiaries, to participate in a real estate investment that he created via the use of trust funds.
- They all agreed, the trustee transferred funds from the four trusts, and the project later failed with the trusts losing $2.1 million.
- In 2011, the trustee filed suit to resign and obtain a judicial discharge, and a sister filed a breach of fiduciary duty claim based on this failed investment.

Trust Dispute For Failed Investments

- Trial court ruled for the trustee, released and discharged him, ruled against sister, and awarded all fees against sister.
- Court of appeals first looked at the statute of limitations and found that it applied to bar the sister's claim.
- The court grouped the sister's various complaints into one barred claim: "Her allegations that Robert lied about the transaction, failed to provide pertinent information about the transaction, and structured the transaction differently than described in his initial email are all facets of the allegation that Robert breached his fiduciary duty by misusing Trust assets for the Bighorn project. Therefore, these allegations share the same accrual date, August 30, 2007."

Trust Dispute For Failed Investments

- The court also affirmed the trustee's affirmative defense of quasi-estoppel: "The affirmative defense of quasi-estoppel precludes a party from asserting, to another's disadvantage, a right inconsistent with a position she has previously taken."
- Trustee initiated approximately fifty real estate transactions in which he invested trust assets, and his sister agreed to all of these transactions.
- All transactions except the one at issue were successful, and the trust benefitted from those prior investments.
- The court held that the sister's claims for breach of fiduciary duty are barred by the affirmative defense of quasi-estoppel.

Trust Dispute For Failed Investments

- The court also affirmed the trustee's exculpatory clause defense.
- The trust provided that the trustee shall not "be held liable for any action or default…, unless caused by his own gross negligence or by a willful commission by him of an act in breach of trust."
- The court affirmed the judgment due to the trustee's testimony about his due diligence, the history of doing successful real estate investments, the consent of the other beneficiaries, his capacity as beneficiary and his loss associated with the investment.
- "There is no evidence that Robert had an actual, subjective awareness of the risk of a coming financial crisis but nevertheless proceeded with conscious indifference to the rights, safety, and welfare of the Trust, his mother, or his sisters. Thus, there is no evidence of gross negligence or a willful commission by Robert of a breach of trust."

Trust Dispute For Failed Investments

- Court reversed the award of the trustee's attorney's fees as against the sister.
- "For purposes of our discussion, a win on affirmative defenses is not on equal footing with a win on the merits. Moreover, neither the Declaratory Judgments Act nor trust code Section 114.064 are prevailing party statutes, and an award of attorney's fees under those statutes is not dependent on a finding that a party substantially prevailed. It follows that Robert's win does not require a determination that an award of attorney's fees is equitable."
- "Considering all of the circumstances, we conclude that it was inequitable as a matter of law for the trial court to order" sister to pay for the trustee's $500,000 in attorney's fees.
- The trust, however, had paid those fees.

Extreme Will Execution

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Extreme Will Execution

- In *Estate of Luce*, the court of appeals affirmed a trial court's admitting a will to probate where the decedent did not personally sign it and only communicated his desires by blinking. No. 02-17-00097-CV, 2018 Tex. App. LEXIS 9341 (Tex. App.—Fort Worth November 15, 2018, op. withdrawn by agr.).
- Paralyzed from the chest down and unable to speak, the testator was able to communicate by blinking his eyes to indicate "yes" and "no."
- Using this blinking system, his attorney was able to draft a will based on the testator's blinked responses to a series of leading questions, and through this system, he directed a notary to sign the will for him.
- After he died, his estranged wife filed an application to probate an earlier will and his sister filed an application to probate the most recent will.

Extreme Will Execution

- Texas Estates Code Section 251.051(2) requires that a will be signed by the testator or by another person on the testator's behalf in the testator's presence and under the testator's direction.
- Texas Government Code Section 406.0165 provides: "A notary may sign the name of an individual who is physically unable to sign or make a mark on a document presented for notarization if directed to do so by that individual, in the presence of a witness who has no legal or equitable interest in any real or personal property that is the subject of, or is affected by, the document being signed."

Extreme Will Execution

- Through the blinking system, the testator confirmed to the attorney that he understood the execution process, that the notary was signing the will for him, and that he was requesting the notary to sign for him.
- Other witnesses to the execution also testified to the soundness of the system and the testator's intent.
- The court of appeals found that this was sufficient evidence to support the finding that the will had been properly executed.
- The court also rejected the wife's mental capacity and undue influence claims.
- The court reversed the trial court's award of attorney's fees to the wife because there was sufficient evidence to support the jury's finding that the wife was not acting in good faith in attempting to probate an earlier will.

Bank Employee Liability

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Bank Employee Liability

- In *Herring v. Am. Paper & Janitorial Prods.*, the plaintiff was a subcontractor who provided janitorial services for a bank and was also a depositor of the bank. No. H-17-3474, 2018 U.S. Dist. LEXIS 215765 (S.D. Tex. December 24, 2018).
- After the plaintiff's representatives were found stealing food after a party, the plaintiff's contract was terminated.
- Later, one of the plaintiff's employees was hired by another company and cleaned the bank's premises.
- The plaintiff sued the bank for breach of fiduciary duty and conspiracy due to the bank's employees' discussions.
- The court granted the bank summary judgment: "Collusion is only illegal if its acknowledged purpose is itself illegal and two people agree. A company cannot conspire with itself. The Bank employees are all members of the Bank, so there could be no conspiracy even if supporting facts existed."

Hiring Counsel

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Hiring Counsel

- In *Pennington v. Fields*, the minority shareholder sued the majority shareholder's attorney and alleged that he committed legal malpractice by, among other things, negligently advising the majority to engage in oppression and breaches of fiduciary duties and that he failed to advise the minority shareholder to protect his interests against the misconduct of the majority. No. 05-17-00321-CV, 2018 Tex. App. LEXIS 6601 (Tex. App.—Dallas August 21, 2018, no pet.).
- The court held that the evidence did not raise a fact issue regarding the existence of an attorney-client relationship and ruled for the lawyers.
- Be very careful regarding your attorney providing advice to other parties (beneficiaries, settlors, etc.). *See Querner v. Rindfuss*, 966 S.W.2d 661, 667-68 (Tex. App.—San Antonio 1998, writ denied) (attorney for executor also owed duties to beneficiaries under facts of case).

Arbitration

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Arbitration

- In *Freeman v. Fid. Brokerage Servs., LLC*, a trustee deposited funds with a brokerage service and signed an agreement. No 3:18-CV-0947-G, 2019 U.S. Dist. LEXIS 34694 (N.D. Tex. March 5, 2019).
- After the trustee died, and his inappropriate use of trust assets was discovered, the beneficiaries sued the brokerage service for aiding and abetting breach of fiduciary duty.
- The brokerage service filed a motion to compel arbitration.
- The federal district court denied the motion: “There is no evidence that the Freemans sought to derive direct benefits from or knowingly exploited the Customer Agreement, embraced the Customer Agreement as nonsignatories but now attempt to repudiate the arbitration clause, or that they brought suit against Fidelity premised on an agreement which includes or is intertwined with an arbitration clause. Here, the Freemans seek to reclaim the monies alleged to have been fraudulently disbursed to Crisler.”

Fiduciary Field

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Conclusion

- Fiduciary issues arise in many different fact patterns—yet, they always interconnect.
- They are ever evolving and changing depending on the mood of the judiciary and legislature.
- The author hopes that this presentation was informative on the recent issues that impact trust/fiduciary relationships.

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