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Recent Cases of Interest to Fiduciaries

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DeRouen v. Bryan, 2012 Tex. App. LEXIS 8635 (Tex. App. 2012)

Trustee not held liable for distributions misappropriated by beneficiary's spouse.

Facts: The trustee of a family trust received three written requests for discretionary distributions signed in the name of the beneficiary. The trustee made each of the requested distributions, totaling roughly $49,000. It was later revealed that the beneficiary's wife had requested the distributions in his name without his knowledge and deposited the distribution checks in their joint bank account. The beneficiary's wife then spent the funds without the beneficiary's knowledge.

Law: A trustee may make distributions only to a trust beneficiary and is liable for distributions made to non-beneficiaries.

Holding: The court ruled that the trustee was not liable for the distributions because the trustee made the distributions to the beneficiary who received actual possession of the distributions when the checks were deposited in his bank account.

Practice Point: Although the court did not find that this trustee had acted improperly in any way, a dispute like this may be avoidable if the trustee holds a meeting or a telephone conference with the beneficiary before making any distributions.

Milton H. Greene Archives, Inc. v. Marilyn Monroe LLC, 692 F.3d 983 (9th Cir. 2012)

In *Marilyn Monroe LLC*, the 9th Circuit Court of Appeals held that the beneficiaries of Marilyn Monroe's estate did not inherit a posthumous right of publicity because Marilyn was domiciled in New York at the time of her death and New York law does not recognize such a right.

Facts: For forty years, the representatives of Marilyn Monroe's estate asserted that at the time of Marilyn's death in California in 1962 she was a domiciliary of New York. Substantial evidence was offered by the representatives of Marilyn's estate to prove her domicile. Marilyn's New York domicile was accepted by several courts and tax authorities and led to the avoidance of California estate tax and successful results in unrelated litigation by the estate in New York courts. Marilyn Monroe LLC, the owner of the residue of Marilyn Monroe's estate, sought to enforce the posthumous right of publicity that exists under California law against Milton H. Greene Archives, Inc., which owned copyrights to Marilyn Monroe photographs. Monroe LLC alleged that Green Archives was violating its rights through the Green Archives' unauthorized use of Marilyn's image and likeness.

Law: California law created a posthumous right of publicity in 1984. New York law does not recognize such a right. In a prior 2007 decision, the New York district court held that California's right of publicity did not apply retroactively to Marilyn's death in 1962. In direct response to this judgment, the California legislature enacted an additional law to apply California's right of publicity to the estates of persons dying prior to 1985.

Holding: Upon reconsideration of the case in light of the amended California law, the district court held in favor of Green Archives and the appellate court affirmed, agreeing that Monroe LLC was judicially estopped from taking the position that Monroe was a California, and not a New York, domiciliary at the time of her death. The court found that until the instant litigation, Monroe's representatives maintained Marilyn was domiciled in New York at her death in all prior judicial proceedings. The doctrine of judicial estoppel bars the same party from taking inconsistent positions in different matters. The court examined the issue of whether sufficient privity existed between Marilyn's estate and Monroe LLC in order to bind the LLC to the positions taken by the estate. The court concluded that Monroe LLC, as the residuary beneficiary of Marilyn's estate, was in privity with the estate and the positions asserted by its representatives. Moreover, the successor representative of Marilyn's estate was also a 75% owner of Monroe LLC and would benefit substantially from a decision against Green Archives. The court concluded that this was a textbook case requiring the application of judicial estoppel.

Practice Point: Not every deceased client will rank among the top names on *Forbes Magazine*'s list of Top-Earning Dead Celebrities as Marilyn did in 2011 with an estimated income of $27 million. Nevertheless, for certain persons with an image whose value is expected to last beyond death, it would be prudent to be domiciled at death in a state like California that recognizes a posthumous right of publicity. Beyond the right of publicity, this case illustrates the importance of clearly documenting a person's domicile where state law considerations, such as state estate tax, can have far-reaching effects on the person's estate and beneficiaries.

In re Stewart, 2012 Ariz. App. LEXIS 158 (Ariz. App. 2012)

An Arizona appellate court upheld the validity of *in terrorem* clauses in the decedent's estate plan documents.

Facts: Thomas Stewart died in 2010 and was survived by five adult children. Prior to his death, Thomas executed a pour-over will and trust which excluded his son Sean as a beneficiary. Thomas' will and trust each included an *in terrorem* clause that provided any person who contested the terms of the will or trust, the acts of the executor or trustee, or Thomas' capacity to execute the documents would be deemed to have predeceased Thomas. The *in terrorem* clause also applied to persons who cooperated or aided a person in contesting the will or trust. Sean sought to invalidate the will and trust and to separately invalidate the *in terrorem* clauses. Sean argued that the *in terrorem* clauses prevented him from engaging in discovery because the clauses prevented the beneficiaries of the will and trust from cooperating or aiding Sean in his litigation.

At a hearing on Sean's claims on the *in terrorem* clauses, the trial court granted Sean's motion that the clauses were invalid under Arizona law and unenforceable on public policy grounds. After Sean settled his remaining claims against his father's estate, the representatives of Thomas' estate appealed, seeking to reverse the lower court's holding that the *in terrorem* clauses were invalid.

Holding: On appeal, the court reversed, finding the *in terrorem* clauses valid because state law did not prohibit *in terrorem* clauses in wills nor did the statute require specific language to make the clauses valid. Instead, the court found that Arizona's statute prevents enforcement of an *in terrorem* clause if probable cause exists to contest the validity of testamentary documents.

The appellate court further rejected the trial court's narrow interpretation of the "no cooperation" part of the *in terrorem* clause as promoting perjury and impeding justice. The appellate court instead read the "no cooperation" part of the clause as requiring forfeiture of a beneficial interest by those beneficiaries who *voluntarily* cooperate with a person challenging an estate plan. Thomas' *in terrorem* clauses were prefaced with the fact that they were to be given effect to the maximum extent permitted by law.

Practice Point: *In terrorem* clauses are valid in many, if not all, states, but will often be narrowly construed. Where guiding state statutes and case law exists, it is a best practice to make sure that such clauses are drafted carefully so as not to exceed the boundaries of state law. In this case, the precatory phrase "to the maximum extent permitted by law" helped the clause to be interpreted as consistent with the state's public policy.

Miami Children's Hospital Foundation v. Miami Care Foundation, 2012 Fla. App. LEXIS 17440 (Fla. 2012)

Trust amendment was not ambiguous as to the testator's intent to benefit the Miami Children's Hospital Foundation.

Facts: Elaine Hillman died in 2007, leaving a pour-over will that distributed her residuary estate to her trust. Elaine's trust was most recently amended in 2004. The dispositive clause at issue provided that 25% of her residuary estate was to be distributed to "Miami Children's Hospital Foundation, Cranial/Facial Foundation [address], att: Dr. Anthony Wolf." Miami Children's Hospital Foundation maintained a craniofacial surgical program and Dr. Wolf was the director of the program at the time the trust amendment was executed. Miami Care was formed in 2006 and Dr. Wolf had become its director at the time of the litigation.

Both Miami Children's Hospital Foundation and Miami Care Foundation received notice of the estate representative's final accounting and petition for discharge. Miami Care objected to the petition, claiming that it was entitled to the distribution under the terms of Elaine's trust. The estate representative sought direction from the court regarding the interpretation of the trust instrument as to which charity was the appropriate recipient of the residuary bequest. The trial court entered an order in favor of Miami Care, finding that the terms of the trust amendment were ambiguous and that Elaine intended Dr. Wolf to control the distribution of the residuary bequest.

Law and Holding: On appeal, the Florida Appellate Court reversed the trial court's holding, finding that there was no ambiguity and that Elaine clearly intended to benefit the Miami Children's Hospital Foundation.

Practice Point: Many charities operate under similar names across the country, and sometimes even in the same geographical area. Drafters of charitable bequests need to be certain of which charity a client intends to benefit and then properly memorialize the bequest in the estate plan so that there is no ambiguity as to which charity should receive estate proceeds.

In re: Estate of Martelli, 2012 Phila. Ct. Comm. Pl. LEXIS 318 (Pa. 2012)

Court removed co-fiduciaries where hostility among the co-fiduciaries resulted in mismanagement of the trusts and estate.

Facts: In his will Giuseppe Martelli established a Marital Trust and a Family Trust for the primary benefit of his wife, Donna Maria, and at his death the assets of both trusts passed to his children. Under the Will, Mr. Martelli named Donna and his sons, Leonard Martelli and Joseph Martelli, to serve as co-executors of the estate and co-trustees of the Marital Trust and the Family Trust. Mr. Martelli died on June 6, 2010. His will was probated on June 8, 2011.

On December 8, 2011, Donna filed three petitions for citations directed at Joseph and Leonard, seeking an account for their administration of the estate and trusts. Leonard and Joseph responded by asserting that Donna had refused to cooperate in the administration of the estate due to mental health problems and at the same time made critical admissions that they had failed to establish estate and trust accounts or to effectively administer the trusts and estate. The court ordered the brothers to file accounts of the estate and trusts with the court. Instead of filing accounts, Leonard and Joseph filed exceptions to the court's decree and sought Donna's removal as co-executor and co-trustee. Donna opposed her removal as fiduciary and advocated that Joseph and Leonard be removed instead.

Law: Removal of a fiduciary selected by the testator is a drastic remedy. Further, in Pennsylvania hostility among co-fiduciaries alone will not justify removal but may be appropriate where it interferes with effective administration of the trust or estate.

Holding: The court held that removal of Leonard and Joseph was warranted where they had admitted that their inability to cooperate with Donna resulted in a failure to establish the requisite accounts and where hostility among the co-fiduciaries resulted in the mismanagement of the estate and trusts.

Practice Point: When drafting documents and considering the appointment of co-fiduciaries, careful consideration should be given to the relationship between the potential co-fiduciaries and any potential conflicts that could arise. Personal feelings that lead to a breakdown in communication or cooperation can result in expensive litigation, and disagreement among co-fiduciaries is not justification for abdicating fiduciaries duties.

Church of the Little Flower v. US Bank, 2012 Ill. App. LEXIS 905 (Ill. App. 2012)

Trustees' fees alone will not justify termination or modification of a trust where contrary to the terms of the trust instrument.

Facts: Erma L. Donelan established a trust for her lifetime benefit. At Erma's death, the trustee was directed to retain $750,000 in trust for the lifetime benefit of Erma's four sisters and upon the death of the survivor of them, retain the assets in further trust for the benefit of three charities – 20% to St. Joseph's Home, 20% to Church of the Little Flower and 60% to Hospital Sisters of St. Francis Foundation. If at any time the value of the trust assets fell below $500,000 the trust was to terminate and the assets were to be distributed outright to the three charitable beneficiaries.

Upon the death of the last to die of Erma's sisters, the trust corpus then exceeding $500,000 was retained in trust for the benefit of the three charities. From 2006 to 2010 the trustee's fees and fund management fees exceeded the 20% beneficiaries' share of the distributions from the trust. Church of the Little Flower filed suit to reform the trust under the doctrine of equitable deviation or *cy pres*, arguing that the trustee's fees and costs which outpaced the distributions to two of the trust beneficiaries substantially frustrated the trust purpose of providing the beneficiaries with useful revenues.

Law: Under the doctrine of equitable deviation a court may modify an administrative or distributive provision of a trust or direct and permit deviation from the trust provision if because of circumstances not anticipated by the settlor, the modification and deviation will further the purposes of the trust. Similarly under the Illinois Charitable Trusts Act, a trust may be terminated if continued administration has become impracticable because of the trust's small size or because of changed circumstances that adversely affect the charitable purpose of the trust.

Holding: The collection of fees by the trustee in excess of the distributions to certain charitable beneficiaries was not unforeseen or a changed circumstance which justified deviation from the trust terms. Further, the trust was not "inherently uneconomic." The court held that in the interest of giving effect to the settlor's intent, the trust could not be terminated. The court noted that there were other ways to address trustee's fees if the beneficiaries deemed them troublesome.

Practice Point: Trustee's fees and costs are inherent in a settlor's choice of a charitable trust as a vehicle to transfer property and, by themselves, do not justify modification or termination of a trust. Depending on the terms of the instrument, removal and replacement of a trustee or challenge to the reasonableness of a trustee's fees may be more appropriate pursuits for beneficiaries frustrated by high fees and costs of administration.

The Sunrise Trust et al. v. Morgan Stanley & Co., Inc. et al., 2012 U.S. Dist. LEXIS 148485 (Nev. 2012)

Court upholds arbitration award dismissing breach of fiduciary duty claim against Morgan Stanley.

Facts: In 2005, Susan King established The Sunrise Trust with herself as the sole beneficiary during her lifetime and her son as sole remainder beneficiary. Ms. King named Allen Spaulding as initial trustee. Mr. Spaulding, as trustee, opened an account in the name of the trust with Morgan Stanley, and Ms. King transferred approximately $150,000 into the account to fund the trust. In 2008, Mr. Spaulding began making withdrawals from the account for his personal use, and by 2009 he had taken substantially all of the account funds. Mr. Spaulding was arrested, found guilty of felony theft, and sentenced to jail.

The trust's account agreement with Morgan Stanley included a provision requiring that disputes related to the account would be submitted to arbitration before the Financial Industry Regulatory Authority ("FINRA"). Ms. King retained counsel and submitted claims against Morgan Stanley and Timothy McElroy, Morgan Stanley's representative for the trust account.

Initial hearing dates were set for April of 2011, but the arbitration panel postponed the hearings until February of 2012 after counsel for the trust requested a postponement due to Ms. King's poor physical condition. As the February hearing date approached, Ms. King's health continued to deteriorate. Just six days prior to the February hearing, counsel for the trust requested a second postponement due to Ms. King's health. The arbitration panel denied this second request, with the understanding that Ms. King could present testimony at a later date. In response, Ms. King stated that she would appear at the hearing on behalf of the trust; the attorney for the trust officially withdrew the day before the hearing.

The arbitration panel conducted the full hearing and issued its award in March of 2012. The panel dismissed Ms. King's claims on behalf of the trust, reaffirming that Mr. Spaulding, and not Morgan Stanley or Timothy McElroy, had a fiduciary duty to the trust and Ms. King. Ms. King filed suit in federal court, seeking to vacate the arbitration award.

Law: Under the Federal Arbitration Act, federal courts may vacate arbitration awards in only four explicitly stated instances. One instance is where the arbitrators were guilty of misconduct in refusing to postpone the arbitration hearing, and another instance is where the arbitrators exceeded their powers or imperfectly executed them. Ms. King argued that the arbitration with Morgan Stanley involved both misconduct and overreaching by the arbitrators.

Holding: The court found that there was no evidence that either the trust or Ms. King was prejudiced by the decision not to postpone the February hearing. At the time of the decision, the trust was represented by counsel and Ms. King's role at the hearing was limited to a short appearance to give testimony as a witness. The impact of Ms. King's poor health on the hearing, to the extent that it prejudiced the trust or Ms. King, was due entirely to Ms. King's decisions to fire the trust's attorney and represent the trust herself, both of which occurred after the panel announced its decision not to postpone the hearing.

The court also found that the arbitrators did not exceed their powers and that Ms. King's arguments on behalf of the trust were really requests to have the court review the panel's factual findings and legal conclusions. The court noted that Ms. King never suggested that the panel acted irrationally in reaching its conclusions. The court also found that the panel did not exhibit manifest disregard for the law because the panel applied the correct law regarding the agreement between the trust and Morgan Stanley, and this was sufficient to preclude any finding of manifest disregard for the law.

Practice Point: As long as the correct process is followed, courts are reluctant to overturn arbitration awards or second-guess the arbitration panel's decisions. Therefore, arbitration provisions are an important shield against liability for financial institutions offering account services to trustees.

DC Comics v. Pac. Pictures Corp., 2012 U.S. Dist. LEXIS 149532 (Cal. 2012)

Royalties Contract Upheld as Binding.

Facts: Superman illustrator, Joseph Shuster, assigned his rights to the Superman comics to DC Comics in 1938 in exchange for lifetime annuity payments. Shuster died in 1992 and was survived by his siblings. Shuster's siblings contacted DC Comics to renegotiate Shuster's annuity agreement with DC. DC agreed to pay the siblings $25,000 per year for their lifetimes in exchange for re-granting all of Shuster's rights in Superman to DC. In 1999, Congress amended copyright laws to allow heirs to terminate copyright assignments occurring before 1978. A child of one of Shuster's siblings sued to terminate Shuster's copyright assignment.

Law: Where parties have clearly expressed their intention that a subsequent agreement supersede a prior agreement, the subsequent agreement extinguishes the old one.

Holding: The new copyright laws allowing for a termination of the assignment are not applicable to Shuster's heirs because the subsequent agreement by Shuster's siblings in 1992 superseded the 1938 assignment. The 1992 agreement contained broad release terms and settled all prior agreements.

Practice Point: Agreements are frequently binding on heirs. Parties negotiating a settlement that will bind future generations should carefully consider whether changes in the law or circumstances may ultimately cause the settled agreement to be less advantageous to either party.

Ames v. Ohle, et al., 2012 La. App. LEXIS 1285 (Louisiana Ct. App. 2012)

Plaintiff's causes of action accrued when she received partial information and the limitations period expired despite concealment by defendant trustee.

Facts: In 1998, Ecetra Ames hired John Ohle, III, to provide tax and financial planning services. In 1999, Ohle began employment with Bank One, an affiliate of J.P. Morgan Chase & Co. That same year, Ames established a CRUT with Ohle as trustee and funded the trust with $5 million, followed by approximately $3 million in contributions over the next two years.

Ohle began misappropriating both the trust funds and Ames' personal funds. In 2001, Ohle convinced Ames to personally invest in a particular hedge fund. After Ames agreed to transfer $5 million for the hedge fund, Ohle invested $4.75 million and took the remaining $250,000 as a fee. At the same time and as trustee of the CRUT, Ohle invested $2 million in the hedge fund and took a fee of $100,000. Ohle collected these fees by having the hedge fund direct funds to a separate bank account held by Ohle. These fees were not disclosed to Ames. Later in 2001, Ohle transferred almost $350,000 of the CRUT's assets to the hedge fund, and then directed the hedge fund to direct that money to Ohle's separate bank account. Ohle then sent approximately $375,000 to the account of Kenneth Brown. Ohle and Brown used the misappropriated fees to fund Brown's position as a third-party investor in a tax strategy sold by Ohle and Bank One. Bank One received significant fees for referring the tax strategy to its clients.

In March of 2003, Ames requested a trust accounting from Ohle. After Ames learned of Ohle's mishandling of trust assets, Ames and Ohle reached a settlement agreement in August 2003. In 2008, Ohle was indicted in New York for various offenses. Ohle's criminal trial revealed details of which Ames was previously unaware.

After an unsuccessful federal lawsuit against Ohle, Bank One, and the other individuals involved in Ohle's scheme, on January 14, 2011, Ames filed a petition in Louisiana court against the same defendants. As part of their defense, the defendants argued that her petition was untimely and barred by the statute of limitations. The Louisiana trial court agreed, and dismissed Ames' petition.

Law: On appeal, Ames made two arguments. First, she argued that some of her claims were subject to a ten-year limitations period, and the trial court erred when it found that they were prescribed solely on the face of her complaint. Second, she argued that the trial court used the wrong standard to determine when her causes of action accrued.

Ames' complaint asserted eight causes of action: violation of Louisiana's anti-racketeering statute; unjust enrichment; breach of fiduciary duty; breach of contract; fraud; detrimental reliance; negligent misrepresentation; and civil conspiracy. The court of appeals reviewed the limitations periods for these actions. Ames' claims for breach of fiduciary duty and breach of contract, negligent misrepresentation, detrimental reliance, and civil conspiracy were all subject to a one-year limitations period. Her racketeering claim was subject to a five-year limitations period. Ames' fraud claim was the sole claim that had a ten-year limitations period. Her unjust enrichment claim was barred because she had other remedies available, which precludes an action for unjust enrichment.

Because most of Ames' claims expired within a year from when her causes of action accrued, Ames argued that the trial court erred in determining when her causes of action accrued. In Louisiana, the limitations period for a cause of action begins to run when the claimant obtains actual constructive knowledge of the facts indicating the cause of action. In 2003, Ames had incomplete knowledge of Ohle's malfeasance when she received the accounting.

The appellate court found that Ames' partial knowledge in 2003 was enough to prompt further inquiry, and should be considered constructive knowledge. Therefore, the limitations period began running in March 2003, and only Ames' fraud claim survived in 2011 when she filed her complaint.

Ames invoked the doctrine of *contra non valentem* and argued that the defendants' acts of concealment and misrepresentations prevented her from discovering her cause of action, thereby tolling the running of the limitations period. In Louisiana, the doctrine of *contra non valentem* applies in four instances, one of which was asserted by Ames: where the defendant has acted to lull the victim into inaction and prevent the victim from bringing the cause of action, the limitation period is suspended until the victim receives actual knowledge of the injury. As the appellate court noted, this doctrine does not apply where the victim's ignorance is attributable to the victim's own unreasonableness. The court found that Ames' acted unreasonably when she failed to make further inquiry into the accounting information given to her by Ohle, and therefore the doctrine of *contra non valentem* was unavailable to her.

Holding: The appellate court affirmed the trial court's dismissal of most of Ames' claims. Most of her claims were long since barred, as they were subject to one-year or five-year limitations periods. Ames should have acted upon the partial knowledge that she received in 2003, and her failure to do so was unreasonable. Ames' fraud claim survived, however, as its limitations period had not yet run.

Practice Point: Partial information concerning a cause of action is sufficient to start the limitations period, and places an affirmative duty on a plaintiff to promptly investigate further and file an action if warranted.