2008

Dealing Fairly With Estate and Trust Beneficiary Complaints

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QUINNIPIAC PROBATE LAW JOURNAL

VOLUME 22 2008 NUMBER 1

ARTICLE

DEALING FAIRLY WITH ESTATE AND TRUST BENEFICIARY COMPLAINTS

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I. INTRODUCTION

The premise set forth in this article is that it is in the interests of all parties[1] to an estate or trust administration that complaints by members of the beneficiary group have a fair hearing. While formal in-court litigation permits a fair hearing where there are large sums and/or wealthy complainants involved, it is not an effective mechanism for "powerless beneficiaries."[2] Various alternative dispute mechanisms,[3] when appropriately employed, can provide a fair hearing; and it is in the best interests of all of the parties that they be used.

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1 For example, testator, executor(s), settlor(s), trustee(s), income beneficiaries.

2 *See* Robert Whitman & Kumar Paturi, *Improving Mechanisms for Resolving Complaints of Powerless Trust Beneficiaries*, 16 QUINNIPIAC PROB. L.J. 64, 70 (2002) [hereinafter Whitman & Paturi, *Improving Mechanisms*] ("By 'powerless trust beneficiaries' reference is made to trust beneficiaries who cannot gain the services of an attorney to carry out the necessary procedural steps required to bring a trustee before the court. The authors conclude that far too often numerous hurdles exist in bringing an action in a state court, resulting in the shielding of an allegedly unscrupulous trustee.").

3 For example, mediation, arbitration. *See* discussion *infra* Part V.

Historically, it has been assumed that the interests of the parties involved in an estate or trust administration are at odds. Traditionally, fiduciary accounting has been left until the end of administration and fiduciary accounting reports have often been voluminous and difficult to comprehend.[4] Now, with technology providing increased flexibility, this need not be the case. The new reality is that upgraded levels of accounting services can be provided. The rising global competition for estate and trust administration business[5] will compel corporate fiduciaries seeking to establish and retain a reputation for excellence to ensure that beneficiaries receive accurate and clear accounting information as promptly as possible. Accordingly, it is in the interest of all of the parties to embrace appropriate, fair and economically efficient procedures. Trust beneficiaries are increasingly more aware of the quality of service offered and are more likely to seek out better service providers. The common modern practice of including provisions in the governing document allowing trustee removal makes this possible.[6]

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[4] Sometimes, the hope was to prevent beneficiaries from asking questions. Section 7-303(c) of the Uniform Probate Code (UPC) reflects this. It only provides that "[u]pon reasonable request, a beneficiary is entitled to a statement of the accounts of the trust annually and on termination of the trust or change of the trustee." UNIF. PROBATE CODE § 7-303(c) (1969), 8(II) U.L.A. 519 (2006). Similarly, under section 813 of the Uniform Trust Code (UTC), the trustee is not required to give the beneficiary information about the trust absent a specific request. UNIF. TRUST CODE § 813 (amended 2004), 7C U.L.A. 609 (2006). In considering many of the UTC provisions, it must be kept in mind that the National Conference of Commissions on Uniform State Laws (NCCUSL) often finds itself between "a rock and a hard place." If it bends too far to protect the interests of the beneficiaries, it faces a lobbying effort to defeat the UTC at the state legislature level. If it bends too far to give in to intense lobbying efforts by the trustees, it produces the clearly watered down type of provisions for fiduciary accounting. This being the case, consideration of a "best practices rule" will often help a practitioner to reach the best result for the client. *See infra* note 13.

If information were provided automatically rather than on request, beneficiaries would be able, by virtue of having pertinent information about their trust, to make informed requests of their fiduciaries as to the proper management and administration of the trust. *See* T.P. Gallanis, *The Trustee's Duty to Inform*, 85 N.C. L. REV. 1595, 1627 (2007) (explaining the importance of the trustee's duty to inform the beneficiary and calling for laws that make the trustee's duty to inform mandatory instead of upon request). Since providing information to the beneficiary is done only upon request and is not mandated by law, some beneficiaries are prevented from asking meaningful questions. *See also* Standish H. Smith, *Reinventing the Corporate Administration of Personal Trusts – A Marketing Opportunity for Banks*, Presentation to the Financial Analysts of Philadelphia, April 20, 2000, at 9, *available at* http://www.heirs.net/downloads/reinventing.pdf. ("[T]rust accounting statements to which I have been exposed do not always appear to be models of clarity or disclosure.").

[5] *See, e.g., Foreign or Domestic, Trust Companies "Virtually Indistinguishable,"* TRUST REGULATORY NEWS, June 2007, at 2 (discussing the increased competition domestic trust companies face as foreign banks establish branches in the U.S. to compete with them).

[6] The UTC's trustee removal provisions have significantly liberalized trustee removal. *See* Alan Newman, *The Intention of the Settlor Under the Uniform Trust Code: Whose Property Is It, Anyway?* 38 AKRON L. REV. 649, 695-98 (2005) (explaining how the UTC's trustee removal provisions significantly expand the common law grounds for changing trustees). For a discussion of how liberal trustee removal procedures permit trust

Furthermore, beyond proper investment and loyalty, the broader, rising concept of "fiduciary duty" requires both a general duty of fairness in all cases and the efficient settlement of unresolved disputes through the suggestion of a proper resolution procedure. This concept makes it essential that beneficiary complaints be dealt with fairly.[7]

II. TRADITIONAL THINKING REGARDING TREATMENT OF BENEFICIARY COMPLAINTS

Early on at common law, the hope was that fiduciaries, having taken an oath, would voluntarily and unselfishly elevate the interests of the beneficiary group above their own in the administration of an estate or trust.[8] Regrettably, experience taught our medieval ancestors that, in some cases, human nature and circumstances thwarted this expectation.[9] At that point, the equity court agreed to hear complaints of the beneficiary group, commencing the process of

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beneficiaries greater freedom and flexibility in "shopping" for a fiduciary, *see* Ronald Chester & Sarah Reid Ziomek, *Removal of Corporate Trustees Under the Uniform Trust Code and Other Current Law: Does a Contractual Lens Help Clarify the Rights of Beneficiaries?* 67 MO. L. REV. 241 (2002).

[7] Trusts scholar John H. Langbein defines fiduciary duty as requiring primarily proper investment and loyalty. He writes, "[a]ll trust fiduciary law rests on two core principles, the care norm (the duty of prudent administration) and the loyalty norm (the duty to administer the trust for the benefit of the beneficiary). The many subrules-for example, the duties to keep and disclose records; to collect, segregate, earmark and protect trust property; to enforce and defend claims; to be impartial among multiple beneficiaries-are all applications of prudence and loyalty." John H. Langbein, *Rise of the Management Trust*, TRUSTS & ESTATES, October 2004, at 54. The duty of loyalty argued for in this article is much broader. This broader fiduciary duty implies that in every situation, the fiduciary has a duty to be honest and fair. To say that a fiduciary's duty to "keep and disclose records; to collect, segregate, earmark and protect trust property; to enforce and defend claims; to be impartial among multiple beneficiaries" and to account in a meaningful and user friendly way are merely "subrules" is to minimize the importance of these duties. For a discussion of proper resolution procedures, *see infra* Part VI.

[8] Originally, uses and trusts were not enforceable in any court but were purely honorary. The performance of the feoffee's duties was voluntary to uses and could not be enforced. *See* GEORGE G. BOGERT & GEORGE T. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 3, at 19-22 (2d ed. 1984) (1965) [hereinafter BOGERT ON TRUSTS]; *see also* AUSTIN W. SCOTT & WILLIAM F. FRATCHER, THE LAW OF TRUSTS 12-14 (4th ed. 1987) (1939) [hereinafter SCOTT ON TRUSTS].

[9] Since early trusts were originally honorary, "[i]f the feoffee to uses saw fit to deny that he held the property for another, and appropriated it to his own use, he might do so with impunity." BOGERT ON TRUSTS, *supra* note 8, § 3, at 21. In medieval times, to curb feudal bloodshed, monks sought to administer sacred oaths known as the "Truce of God" whereby the oath taker foreswore violence against certain classes of people and property or on certain days of the week. These oaths were routinely broken when they no longer served the interests of the warlords. *See* RODULFUS GLABER, THE FIVE BOOKS OF THE HISTORIES (John France ed., Clarendon Press 1989).

in-court formal litigation to remedy breaches of fiduciary duty.[10]

In those bygone days, being that few individuals died with substantial wealth, the formal, in-court litigation process served reasonably well to monitor claims of breach of fiduciary duty. Later, when corporate entities were allowed to serve as fiduciaries for a fee[11] and many more persons died with wealth, estate and trust administration grew into a profitable and complex business.[12] As the power of corporate fiduciaries grew in the United States, they came to represent a powerful lobby. As a result, legislation favoring corporate fiduciaries was widely enacted.[13] Beyond that, corrupt practices grew

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[10] Once it became clear that trustees could not be relied on to keep their promises, "beneficiaries of uses alleging loss due to a failure of the feoffees to uses to hold the property for their use should apply to the chancellor for relief. At some time early in the fifteenth century the justice of these petitions began to be recognized by the chancellor, and uses and trusts were enforced." BOGERT ON TRUSTS, *supra* note 8, § 3, at 22.

[11] Originally, only individuals could serve as trustees and were not allowed to charge fees for their services. See SCOTT ON TRUSTS, *supra* note 8, § 1.8, at 27-28. "The great contribution made by America to the development of the trust is in the employment of the corporate trustee. In England as late as 1743, the Attorney-General argued that a corporation could not be a trustee. Lord Chancellor Hardwicke, however, told the Attorney-General that nothing was clearer than that corporations might be trustees. The earliest instance in the United States of a specific grant to a corporation of the power to act as trustee seems to have been that of the Farmers' Fire Insurance & Loan Company, chartered in New York in 1822. Since that time, the creation of corporations with power to administer trusts has become increasingly common. The Congress finally found it necessary to permit national banks to enjoy similar powers. Although the corporate trustee is primarily an American institution, the institution is spreading to other countries, and even in the more conservative mother country the corporate trustee is becoming common. . . . In England, the individual trustee receives no compensation for his work, unless it is otherwise provided by the trust instrument. In the United States, however, he [uniformly] receives compensation." *Id.* (internal citation omitted). *See also* Robert Whitman, *Resolution Procedures to Resolve Trust Beneficiary Complaints*, 39 REAL PROP. PROB. & TR. J. 829, 844 (2005).

[12] SCOTT ON TRUSTS, *supra* note 8, § 1.8, at 28. "In the United States, however, [the trustee] receives compensation. The result is that in the older communities it is not uncommon to find men who make a profession of acting as trustees. The trust companies and banks that have trust powers are of course professional trustees; they are in the business of administering trusts." *Id.*

[13] *See generally* Standish H. Smith, *Reforming the Corporate Administration of Personal Trusts - The Problem and a Plan*, 14 QUINNIPIAC PROB. L.J. 563, 564-65 (2000) ("[T]he legal playing field between a corporate trustee and the beneficiaries of a personal trust can be unbalanced in favor of the former, a situation which is sometimes exploited by banks to a point that may at times compromise a corporate trustee's duty of loyalty." Smith argues that changes to the current law must be made to offset existing "federal and state law that serve the banking interests, but not necessarily those of the consumer, and . . . prevent the industry from continuing to use its deep pockets and financial sophistication in a manner sometimes detrimental to beneficiaries."). Many commentators conclude that the NCCUSL is strongly influenced by powerful lobbying groups. These authors contend that politics influence the NCCUSL and that rules are adopted when and because interest groups influence the process. *See, e.g.*, Alan Schwartz & Robert E. Scott, *The Political Economy of Private Legislatures*, 143 U. PA. L. REV. 595, 597 (1995) ("These . . . rules ordinarily advance the interest group's agenda."); *see also* Frances H. Foster, *Trust Privacy*, 93 CORNELL L. REV. 555, 573-74 (2008) (recent trends suggest that beneficiaries have begun to lobby for

because all fiduciaries were placed in a position where they could be tempted to place their own interests over those of the beneficiary group. These corrupt practices developed as a way to enrich fiduciaries at the expense of beneficiary groups that were not organized in a manner that would allow them to balance the power exerted by fiduciaries and their counsel. Consequently, the public developed a fear of getting involved with lawyers, fiduciaries, and the probate system generally.[14]

Whereas wealthy beneficiaries can still afford to protect their interests by retaining counsel and litigating in court, poorer beneficiaries with smaller claims often find themselves barred from any form of redress for claimed wrongs.

III. WHY POWERLESS BENEFICIARIES TODAY MAY NOT BE ABLE TO RECEIVE A FAIR HEARING OF THEIR COMPLAINT

If a complaining beneficiary is "powerless"[15] and/or the complaint is not for a large amount, it may not be possible to retain a lawyer to represent the beneficiary. The beneficiary is unable to pay an attorney on an hourly rate basis and the amount at issue will make a contingent fee arrangement unattractive to the attorney. Furthermore, in situations where the corporate fiduciary is a major bank in the area, attorneys may choose not to take the case because of

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new legislation to reduce power of trustees in existing probate law).

Statutory provisions governing trustee removal made removal difficult. *See* Charles E. Rounds, Jr., LORING: A TRUSTEE'S HANDBOOK § 7.2.3.6 (2003) [hereinafter LORING] (quoting UNIF. TRUST CODE § 706 cmt.) ("Removal may be ordered because of hostility between the trustee and a beneficiary, but only in rare cases. [R]emoval . . . [, for example,] . . . might be justified if a communications breakdown is caused by the trustee or appears to be incurable. On the other hand, relief has been denied if the trustee's duties are essentially ministerial or if the proper administration of the trust is not jeopardized by the hostility." (internal quotation marks omitted) (alteration in original)). This, in turn, made it common for draftsmen to provide for literal removal provisions in the governing instrument.

[14] It is quite common to hear dissatisfaction voiced concerning the capability of fiduciaries. *See* Joel C. Dobris, *Changes in the Role and the Form of the Trust at the New Millennium, or, We Don't Have to Think of England Anymore*, 62 ALB. L. REV. 543, 549 (1998) ("[I]t seems that fiduciary duty, or to speak more broadly, fiduciary responsibility, is losing some of its power as an organizing principle in the trust world. Fewer and fewer people believe in fiduciary duty, unless someone is watching. . . . Stating it more broadly, one could fill a hall with people who would say the traditional doctrine of trustee duty and accountability is more moth-eaten than it is modern."); *see also* NORMAN F. DACEY, HOW TO AVOID PROBATE (1st ed. 1980); *see also* Robert Whitman, *Disclosure Strategies to Settle Complaints and Avoid Formal Litigation*, SK089 ALI-ABA 481, 486((Feb. 10-11, 2005) ("Just one complaint that is NOT FAIRLY HEARD can have enormous fall out in providing the public with a negative feeling for the entire estate and trust system.").

[15] *See supra* note 2.

conflicts or fear that they will lose future business.[16]

It is most likely that in the majority of estate and trust administrations occurring in the United States today, fiduciaries and their counsel act responsibly and treat members of the beneficiary group fairly. The reality, however, of estate and trust administration is that it often presents difficult issues in which the interests of a fiduciary and the members of the beneficiary group clash. As such, a proper balanced resolution of the issues presented is, at times, unclear. Various members of the beneficiary group may have opposing interests and issues may arise concerning the interpretation of the governing instrument, use of discretionary authority, reasonableness of fees, prudent investment and diversification, etc.

It is not clear exactly how many beneficiary complaints arise annually in the United States. Of those complaints, it is unknown what percentage are totally unfounded, border on being justified, or will likely be found to be justified if a fair hearing takes place. Given the volume of trust business as compared to the known level of complaints, it seems evident that most often, complaints do not arise. But what is equally apparent is that, particularly when a major corporate fiduciary is involved, a "powerless beneficiary" asserting a relatively small claim may be unable to retain the services of a competent lawyer to represent the beneficiary's interests. Consequently, the beneficiary may be denied a fair hearing of the complaint.

IV. THE FIDUCIARY'S INTERNAL PROCESS OF RESOLUTION

In many cases, a fiduciary's prompt response to a beneficiary's complaint can lead to its prompt resolution. Often, the beneficiary group may lack an understanding of the circumstances or the various competing factors that the fiduciary needs to consider in making decisions.[17]

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[16] *See* Whitman & Paturi, *Improving Mechanisms*, *supra* note 2, at 77.

[17] BOGERT ON TRUSTS, *supra* note 8, § 961, at 2, 4 ("That the settlor has created a trust and thus required that the beneficiary enjoy his property interest indirectly does not imply that the beneficiary is to be kept in ignorance of the trust, the nature of the trust property and the details of its administration . . . it is the duty of the trustee to give the beneficiary the information which he has asked."); *see also* Jo Ann Engelhardt & Robert W. Whitman, *Administration with Attitude: When to Talk, When to Walk*, PROB. & PROP., May-June 2002, at 13 ("The consensus is that if the fiduciary can improve its communications, it will avoid many problems and mitigate antagonism among the parties if problems occur."); Robert Whitman, *Disclosure Strategies to Settle Complaints and Avoid Formal Litigation*, SK089 ALI-ABA 481, 514 (Appendix D) (Feb. 10-11 2005) (response of James Wade stating, "[i]t has been my experience that most disputes between beneficiaries and trustees are a result of poor communication, particularly a failure on the part of the trustee to see that the

Because a fiduciary is bound by fiduciary law to place the interests of the beneficiary above its own, failing to communicate effectively or displaying a lack of interest in seeing that the beneficiary's concerns are promptly and fully addressed appears to constitute an independent breach of fiduciary duty, separate from the original complaint. Beneficiaries who are ignored become irate and overly suspicious.[18] Ideally, at the outset of administration,[19] every fiduciary will outline to the beneficiary the fiduciary's written policies for internally resolving disputes, so as to minimize confusion and conflict.

V. THE IMPORTANCE OF ALTERNATIVE DISPUTE RESOLUTION

In situations where formal, in-court litigation may not be feasible in practice, alternative dispute resolution becomes important. While beneficiaries opting for formal litigation should never be prevented from taking that route, it is most important that a complaining beneficiary understand: 1) the internal process of resolution available to the fiduciary, 2) the fiduciary's written policies with regard to providing a "proper resolution process," and 3) the

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beneficiary understands the ground rules for estate and trust administration (including such items as pass through to the beneficiary of trust income, how charges for trustee and other administration expenses are charged against income or principal or a combination, and how investment receipts are allocated as between the principal and income accounts)").

[18] Whitman, *supra* note 11, at 838 ("For example, consider the plight of *RK*, a trust beneficiary who sought an accounting from her out-of-state trustees. *RK* believed she was entitled to approximately $30,000. After consistent stonewalling, *RK* sent the trustees a letter in which, because of her total frustration, she accused them of being 'crooks' (which they may well have been). The trustees counterclaimed for defamation and received a default judgment against *RK* in their home state. *RK* could not afford to travel to court to defend herself. The judgment, by an allegedly 'friendly' judge, was for $2,000,000."); *see also* Robert Whitman, *Sorting Out Receipts and Releases*, 33 ACTEC J. 142, 143 (2007) ("Heavy-handed negotiating strategies, such as giving unreasonable ultimatums, may totally undermine goodwill. As an example, a trustee who requires the execution of [a] R[eceipt] and R[elease] without disclosing how much the beneficiary can expect at the distribution and the amount of trustee fees should expect the beneficiary to be cautious and suspicious.").

[19] Engelhardt, *supra* note 17, at 13 ("Many commentators recommend that a fiduciary present a written summary of the trust terms and a statement of both the fiduciary's duties and responsibilities and the beneficiary's rights and remedies at the beginning of the relationship. This lets the beneficiary know what to expect and allows the fiduciary to manage the beneficiary's expectations."); *see also* Robert Whitman, *Sorting Out Receipts and Releases*, SN003 ALI-ABA 281, § 1.3, at 288 (July 19-20 2007) ("The beginning of the fiduciary relationship presents significant tactical opportunities for fiduciaries to advise the beneficiary group regarding what will be happening at various stages of the administration. Hopefully, from the outset, the beneficiary group has no distrust, nor suspicion concerning the fiduciary. The fiduciary, at the beginning of the relationship, can review numerous administrative and procedural matters, outlining the benefits and responsibilities arising pursuant to the new fiduciary relationship. Presenting a clear picture of what will be coming avoids later unexpected surprises.").

beneficiary's right to participate in the process of designing a proper resolution process.

VI. FIDUCIARY POLICIES REGARDING PROPER RESOLUTION PROCEDURES

If standard internal processes of resolution cannot resolve a beneficiary complaint and the beneficiary does not opt for formal litigation, the stage is set for the fiduciary to put into effect the fiduciary's policy regarding the creation of a "proper resolution procedure."

Arguably, to meet a fiduciary's duty, every fiduciary must have a written form of policies in place outlining the steps to be taken to establish a "proper resolution procedure."[20] Ideally, the fiduciary should have disclosed these procedures to all members of the beneficiary group at the outset of administration.[21]

Among the goals to be reached in formulating the fiduciary's policies should be the goal of allowing the beneficiary to work with the fiduciary in choosing the particular plan to be established to resolve the matter. Depending on the circumstances of the case, arbitration, mediation, the appointment of an independent resolution officer, or any combination of the above mechanisms that appear to meet the needs of the parties in a balanced way should be made available.[22]

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[20] *See* Donald P. DiCarlo, Jr., *Using Fiduciary Procedures to Build Beneficiary Buy-In,* SK004 ALI-ABA 53, 56 (July 1-2, 2004) (calling for reforms aimed at increasing the amount of beneficiary and trustee cooperation by establishing mediation procedures to resolve potential conflicts and creating a system for the beneficiary to provide the trustee with both negative and positive feedback on the current administration of the trust); *see also* Robert Whitman, *Flexible Fiduciary Accounting from the Outset of Administration*, PROB. & PROP., May-June 2004, at 45.

[21] *See* RESTATEMENT (SECOND) OF TRUSTS § 170(2) (1959) ("The trustee, in dealing with the beneficiary on the trustee's own account, is under a duty to the beneficiary to deal fairly with him and to communicate to him all material facts in connection with the transaction which the trustee knows or should know.").

[22] Whitman & Paturi, *Improving Mechanisms*, supra note 2, at 72 n. 12 ("[T]he authors [argue for] the possibility of a broad-based voluntary system for trust beneficiary insurance that would give powerless trust beneficiaries early access to competent legal advice. Another possibility would be for trustees to voluntarily set up independent fact finding agencies to resolve complaints by mediation and/or arbitration."); *see also* Bridget A. Logstrom, Bruce M. Stone & Robert W. Goldman, *Resolving Disputes with Ease and Grace*, 31 ACTEC J. 235, 236-37 (2005) (elucidating the advantages of arbitration of trust & estate disputes as opposed to formal, in-court litigation, among which include the reduced cost and time of arbitration and the benefit of allowing the parties to tailor the arbitration procedure according to the needs of their specific dispute).

VII. SHOULD AN ATTEMPT BE MADE TO DRAFT A PROPER RESOLUTION PROCEDURE INTO THE GOVERNING DOCUMENT?

Since it is impossible to predict the kinds of problems that will arise in the future, the only provision that need be drafted into the governing instrument should be the following:

> If a dispute arises between the fiduciary and/or one or more members of the beneficiary group, the fiduciary shall work with the complainant to adopt a proper resolution procedure in order to promptly and economically resolve the dispute.

An attempt to set out more rigid procedures in the governing document will likely be counterproductive. No one can accurately anticipate the set of circumstances that may come to exist at the time when the complaint arises.

VIII. CONCLUSION

Practices in which politically strong groups representing fiduciaries lobby for legislation to protect their interests and leave other interested groups, such as trust beneficiaries, unprotected fail to maximize the public's acceptance and endorsement of our estate and trust administration system in the long term. Global competition will compel the United States to reorganize its estate and trust administration systems if it is to retain a leadership position. It is in the long term interests of all of the parties to seek a balanced system that allows for a fair hearing of beneficiary complaints.