



## Texas Fiduciary Litigation Update 2013-2014

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# Introduction

- Financial institutions are routinely called upon to take fiduciary roles in managing assets.
- This role can require the fiduciary to act and file suits, and it can also open the fiduciary up to potential liability.
- This presentation is intended to provide an update on current legal precedent that impacts fiduciaries.

# Trust Modifications

- *In re Hubberd Testamentary Trust*, No. 04-13-00452-CV, 2014 Tex. App. LEXIS 1493 (Tex. App.—San Antonio February 12, 2014).
- A party appealed from a court's order modifying a trust based on a mediated settlement agreement.
- The appealing party argued that the trial court erred because Texas Property Code section 112.054(d) prohibits a court from taking action under section 112.054(a)(5) unless all beneficiaries have consented to the order.
- Court of appeals held that section 112.054(d) did not apply as the application to modify the trust was filed under sections 112.054(a)(2) and (a)(3).

# Trust Modifications

- Under sections 112.054(a)(2) and (a)(3), a court is authorized to modify the terms of the trust if: 1) because of circumstances not known to or anticipated by the settlor, the order will further the purposes of the trust; or 2) modification of the administrative, nondispositive terms is necessary to prevent waste or avoid impairment of the trust's administration.

# Trust Modifications

- To determine if the modifications were appropriate, the court had to determine the purpose of the trust.
- They were: 1) to unconditionally distribute all income to the income beneficiaries; and 2) to distribute principal as necessary to provide adequately for the health, support, education, or maintenance of the appellant and the other beneficiaries.

# Trust Modifications

- Trial court modified the trust to require appellant to obtain health and general liability insurance.
- Court of appeals affirmed this modification, as the settlor could not have anticipated that the beneficiary would refuse to obtain such insurance and the requirement supported the purpose of the trust.

# Trust Modifications

- The trial court also required that premiums for the insurance be paid from trust income and allowed the trustee to withhold principal distributions if insurance was not maintained.
- The court of appeals reversed this aspect of the modification because it would not further the purpose of distributing the “entire net income” from the trust to appellant and would subvert the goal of caring for the appellant.

# Spousal Right To Trust Distributions

- *In re BancorpSouth Bank*, No. 05-14-00294-CV, 2014 Tex. App. LEXIS 4052 (Tex. App.—Dallas April 14, 2014).
- In a divorce proceeding of a beneficiary of a spendthrift trust, a trial court ordered a trustee to make mandatory distributions to the beneficiary's wife as spousal support and to make discretionary distributions to the registry of the court.

# Spousal Right To Trust Distributions

- Bank/trustee filed a mandamus proceeding challenging the order.
- The court of appeals held that the trustee had standing to do so: “the trial court has ordered relator, a non-party to the case, to take actions that relator believes are inconsistent with its obligations as trustee. Accordingly, relator may pursue ... a mandamus.”

# Spousal Right To Trust Distributions

- The court of appeals granted mandamus relief, reversing the trial court's order.
- Spendthrift trusts are trusts with language prohibiting the voluntary or involuntary alienation of the beneficial interest.
- They protect a beneficiary from his creditors by expressly forbidding alienation of the beneficiary's interest.

# Spousal Right To Trust Distributions

- Spendthrift trusts are not enforced out of consideration for the beneficiary, but rather, so that the settlor can control her bounty and secure its application according to her pleasure.
- There are no statutes that allow a trial court to redirect payments from a spendthrift trust to a spouse or former spouse.

# Spousal Right To Trust Distributions

- Texas Family Code section 154.005 provides that a court may order a trustee of a spendthrift trust to make disbursements for the support of a child to the extent that the trustee is required to make payments to a beneficiary who is required to make child support payments.
- Court held that this statute was inapplicable to spousal support.

# Spousal Right To Trust Distributions

- *Benavides v. Mathis*, No. 04-13-00186-CV, 2014 Tex. App. LEXIS 1488 (Tex. App.— San Antonio February 12, 2014)
- *Benavides v. Mathis*, No. 04-13-00270-CV, 2014 Tex. App. LEXIS 3233 (Tex. App.— San Antonio March 26, 2014).
- Beneficiary of trust was incapacitated and had a guardian appointed.

# Spousal Right To Trust Distributions

- Guardian and trustees determined that trust distributions were beneficiary's separate property and denied beneficiary's wife's request for half of the distributions.
- Separate property consists of the property owned or claimed by the spouse before marriage, acquired during marriage by gift, devise, or descent, and the recovery for personal injuries.

# Spousal Right To Trust Distributions

- Courts have generally held that distributions of trust income from a testamentary or inter vivos trust to married recipients who have no present, possessory interest to the trust corpus are separate property.
- Court of appeals determined that, even though the irrevocable trust could be amended, it was still irrevocable.

# Spousal Right To Trust Distributions

- Court of appeals also held that the beneficiary did not have a present, possessory interest in the trust corpus.
- Court concluded that the beneficiary did not receive corpus, but only income from the trust because the trust defined royalties and bonuses as income.
- Beneficiary's limited right to transfer interest also did not mean that he had a present, possessory interest.
- Trial court correctly entered summary judgment for the guardians on wife's claims of breach of fiduciary duty, tortious interference, and other related tort claims.

# Gender/Spousal Issues

- *In re Estate of Araguz*, No. 13-11-00490-CV, 2014 Tex. App. LEXIS 1573 (Tex. App.—Corpus Christi February 13, 2014, pet. filed).
- Tom married Heather and had children.
- After Tom divorced Heather, he married Nikki.
- Shortly after that marriage, Tom died in the line of duty as a firefighter.

# Gender/Spousal Issues

- After Tom died, his mother and Heather filed suit to declare Tom's marriage to Nikki void on the ground that it was an illegal, same-sex marriage.
- Nikki was born as "Justin Graham Purdue" in California, but had lived most of her life as a girl as she had been diagnosed with "gender dysphoria."
- At age 21, Nikki filed suit to obtain a name change, which a Texas court granted.
- She then obtained a new birth certificate with her new name, a Kansas driver's license listing her as a female, and a new Texas license listing her as female.
- At the time that Tom and Nikki were married in Texas and obtained a marriage license, Nikki still had male genitalia but she later a sex change operation.
- After Tom's death, she obtained a new California birth certificate listing her as a female.

# Gender/Spousal Issues

- The trial court ruled for Mother and Heather based on *Littleton v. Prange*, 9 S.W.3d 223 (Tex. App.—San Antonio 1999, pet. denied).
- *Littleton* held that Texas law does not recognize any individuals “as having successfully changed their sex.”
- If you were born a male, you could not change your sex.

# Gender/Spousal Issues

- Texas law is very clear that marriage is solely between one man and one woman, and same-sex marriages are contrary to public policy.
- So, a marriage license cannot be issued to persons of the same sex and an informal (or common-law) marriage may not exist between persons of the same sex.

# Gender/Spousal Issues

- So, if Nikki were a man at the time that she married Tom, the marriage was void.
- As Tom had no will, that would greatly impact the identity of Tom's heirs and who would receive under his estate.
- The court of appeals reversed the trial court's judgment and held that there was a fact issue regarding Nikki's sex.

# Gender/Spousal Issues

- In 2009, the legislature amended the family code to add a court order related to an applicant's "sex change" as a form of acceptable proof to establish an applicant's "identity" and age, and thus, eligibility, to obtain a marriage license.
- Court held that "Texas law recognizes that an individual who has had a sex change is eligible to marry a person of the opposite sex."

# Gender/Spousal Issues

- Court then cited at length from Nikki's expert report.
- A doctor stated that the factors that should be taken into account when identifying someone as male or female include chromosomes, hormones, sexual anatomy, gender identity, sexual orientation, and sexual expression.
- He also noted that while sexual anatomy at birth is typically the basis for determining an individual's sex, this is sometimes done incorrectly.

# Gender/Spousal Issues

- The expert concluded: “Surgery per se is not the definitive point that makes someone female. Rather, it is completion of the real life experience which documents . . . [that] she had this condition at birth, recognized such as she grew up, and took the steps to resolve this issue. And, she pursued the transition in accordance with The Standards of Care of the World Professional Association for Transgender Health; I regard her medically and psychologically as female.

# Gender/Spousal Issues

- Court held that this evidence created a fact issue as to Nikki's gender at the time of marriage.
- On the other side, the court concluded: "Heather and [the Mother's] evidence showed that Nikki had male sex organs during the marriage. In our view, this was enough to raise a fact issue about whether Nikki was male during the marriage because a rational trier of fact could draw a reasonable inference that Nikki was male based on her male sex organs."

# Gender/Spousal Issues

- The Mother and Heather filed a petition for review with the Texas Supreme Court, and it is currently pending.
- How does this impact a financial institution's practice?
- Interpreting wills with the term: "spouse"
- A "spouse's" right to community property for determining a trust's property.

# Will Interpretation

- *Stephens v. Beard*, No. 12-13-00160-CV, 2014 Tex. App. LEXIS 3895 (Tex. App.—Tyler April 10, 2014).
- Husband shot his wife, who died immediately, and then shot himself. He died hours later in the hospital.
- Their wills provided for nine cash bequests if they died in a common disaster or under circumstances making it impossible to determine who died first.

# Will Interpretation

- Executrix claimed that nine specific bequests were not triggered because she could tell who died first and it was not a common disaster.
- The court of appeals held that it was a common disaster: “the shots were fired in one episode, which is a common disaster in spite of the fact that [husband] did not successfully kill himself immediately.”

# Will Interpretation

- Court also looked at the application of the Simultaneous Death Act, which provides that a person who dies less than 120 hours after the time the decedent dies is deemed to have predeceased him and therefore cannot be a beneficiary.
- This is a default rule, and testators can direct a different result.

# Will Interpretation

- In the provisions of the will where the testator specified that the devise was contingent on the decedent's spouse surviving the decedent by ninety days, the Act did not apply.
- Regarding the “die in a common disaster” provision, the Act did apply as it was consistent with the Act.

# Claims Against Estate Representatives

- *Diaz v. Elkin*, No. 01-13-00500, 2014 Tex. App. LEXIS 4317 (Tex. App.—Houston [1st Dist.] April 22, 2014).
- Defendant was an executrix of an estate in Peru (decedent also created will in Peru).
- Beneficiaries filed suit in Texas for breach of fiduciary duty.

# Claims Against Estate Representatives

- Executrix filed a plea to the jurisdiction, which the trial court granted.
- As a general rule, Texas courts have no jurisdiction over a representative of an estate who holds that status by virtue of an appointment in another state or jurisdiction.
- Beneficiaries argued that jurisdiction existed because they were suing the executrix solely in her individual capacity for money damages.

# Claims Against Estate Representatives

- Court of appeals disagreed and affirmed the trial court's dismissal.
- Beneficiaries' breach of fiduciary duty claim was solely based on the executrix's role as the representative of the estate.
- Further, the beneficiaries sought money damages, which were inextricably tied to the estate's assets and the administration of the same, not to assets held by executrix in her personal capacity.

# Claims By Trustees

- In *Rice v. Malouf*, a former co-trustee, acting alone without the knowledge of his co-trustee, caused \$1.6 million dollars to be transferred by wire from a trust bank account to the recipient's account.
- Other co-trustees later filed suit against the recipient for a constructive trust and sought the return of the money.

# Claims By Trustees

- Section 284 of the Restatement of Trusts states that when a trustee in breach of trust transfers trust property to a person who takes it "for value" and "without knowledge of a breach of trust," the latter holds the interest free of the trust and is under no liability to the beneficiary.
- Issue in case was whether the transfer was "for value."

# Claims By Trustees

- The court of appeals affirmed the jury's verdict that the transfer was "for value."
- The co-trustee who transferred the money had an entity that owed \$1.7 million to the recipient's businesses.
- The court held that the recipient of the funds was allowed to keep those funds.

# Joint Account

- *Mims – Brown v. Brown*, No. 05-12-01132-CV, 2014 Tex. App. LEXIS 3754 (Tex. App.—Dallas, March 31, 2014).
- Mother was the executrix of father's estate and distributed real property to the son.
- The son sold the property and deposited the proceeds into an account called "JTWROS" with the mother as co-applicant in 2003.

# Joint Account

- The account agreement had no language describing what JTWRORS was but stated that the bank could amend the agreement in the future without notice.
- In 2007, the bank amended the agreement to have an adequate legal description for “JTWRORS.”
- In 2008, the son died, and the mother received the proceeds from the account.

# Joint Account

- The son's wife sued the mother for the funds, and the court held that the bank's amendment and addition of adequate "JTWRORS" language was effective.
- Court also held that Probate Code § 440 did not apply because the son and mother were not trying to change the account.
- Section 440 states that a JTWRORS form may be altered by written order given by a party to the banks and that the order must be signed by the party and received by the bank during the party's lifetime.

# Joint Account

- The son's wife also alleged that the mother breached fiduciary duties as she was the executrix and the son was a beneficiary.
- The court held that the mother did not breach a fiduciary duty by entering into the account agreement with the son.
- The court held that after the land was distributed to the son, it was no longer a part of the estate.
- When the mother signed the account agreement and received the proceeds, neither "occurred in the context of" the administration of the estate.
- The court found no law that would continue the fiduciary's obligation with regard to estate property years after it was distributed and after it had changed to a non-probate asset.

# Trustee Standing

- *Lombona v. AIG Am.*, No. 01-12-00168-CV, 2014 Tex. App. LEXIS 2302 (Tex. App.—Houston [1st Dist.] February 27, 2014).
- After the beneficiary of a trust died, an insurance company refused to pay life insurance proceeds to the trust.
- The trustee filed suit, and the defendant alleged that the trustee did not have standing because the trust terminated.

# Trustee Standing

- During a trust's existence, legal title is held by the trustee but equitable title is held by the beneficiaries.
- When an event happens to terminate a trust, i.e., death of beneficiary, then the two merge into the beneficiaries.
- However, the trustee retains power to wind up the affairs of the trust or to distribute the trust property in accordance with the terms of the trust.

# Trustee Standing

- The trustee was also the trustee of the remainder beneficiary trusts – so she had standing either way.
- Because the trustee failed to pay the premium for a year, the insurance company was not obligated to pay the proceeds to the trustee.

# Venue

- *In re Wheeler*, No. 10-13-00402-CV, 2014 Tex. App. LEXIS 1065 (Tex. App.—Waco January 30, 2014).
- Purchaser of real property interests sued a trustee over the sale agreement in the county where the property was located.
- The trustee filed a motion to transfer venue to the county where the trust was administered under or Texas Property Code Sections 115.002 and 115.001.

# Venue

- The trial court denied the motion, but the court of appeals granted mandamus relief for the trustee.
- Section 115.002 states that venue of an action should be brought in the county in which the trustee resided during the last four years or the situs of the administration of the trust for that time period.
- Section 115.001 includes all proceedings by or against a trustee and all proceedings concerning trusts.
- This mandatory venue provision controlled and required suit to be moved.
- Note there is a split in the court of appeals on this issue.

# Attorney/Client Privilege

- *In re Segner*, No. 05-13-01414-CV, 2013 Tex. App. Lexis 14796 (Tex. App.—Dallas December 5, 2013).
- Trustee hired consultant to assist in the management of a trust, including supervising employees and assisting with attorneys.
- In litigation, the trustee designated the consultant as an expert and disclosed his file and everything that was provided to him, reviewed by, prepared by, or prepared for him “in anticipation of his expert testimony.”

# Attorney/Client Privilege

- The opposing party sought production of much broader information from the consultant, which the trial court granted.
- The court of appeals granted mandamus relief because the information was protected by the attorney/client privilege.
- The court focused on the consultant's testimony, that he "sent and reviewed confidential communications with the trust's attorneys for the purposes of effectuating legal representation for the trust."

# Conclusion

- Fiduciary litigation is an ever changing field.
- The law expands and contracts depending on the mood of the Legislature and judiciary.
- The author hopes that this update provides assistance to financial institutions that choose to take on fiduciary duties.