



## Texas Fiduciary Litigation Update 2015-2016

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# Introduction

- Fiduciary litigation is an ever changing area in the law.
- Author reviews new cases regularly and has a blog: [Texas Fiduciary Litigator \(Txfiduciarylitigator.com\)](http://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.

# Fun Case

- In *Markl v. Leake*, No. 05-15-00455-CV, 2015 Tex. App. LEXIS 11261 (Tex. App.—Dallas Nov. 2, 2015, no pet.).
- A husband started a long-time extramarital relationship with his girlfriend in 2004.
- The husband gave her money, placed her on the payroll of his business, provided her a credit card, and maintained her vehicle and real property.
- The husband invested approximately \$35,000 in his girlfriend's real properties.

# Fun Case

- The relationship ended when the girlfriend caused the husband to be indicted for four felony charges related to an “altercation” and obtained a protective order prohibiting his entry upon her real property.
- The husband and wife then sued the girlfriend for breach of fiduciary duty and other tort claims arising from the benefits bestowed upon her during the relationship.
- They sought a temporary injunction to prevent the girlfriend from disposing of the two parcels of real property in which they purportedly invested money.
- The trial court denied the injunction, and the husband and wife appealed.

# Fun Case

- The court noted that it had located no authority recognizing a fiduciary relationship between the wife of a husband involved in an extramarital affair and the woman with whom the husband was carrying on that affair.
- The court affirmed the trial court's finding that the girlfriend did not owe any such duty to the wife.

# Fun Case

- The court held that while a marital relationship is a fiduciary one, that the relationship of girlfriend and boyfriend, without more, is generally not a fiduciary relationship.
- Once again, the court could not find any authority declaring the existence of a fiduciary relationship based on an extramarital affair.
- Longstanding romantic and sexual relationship does not create fiduciary duties.
- The husband's expenditures merely demonstrated donative gifting of labor and money to a girlfriend and did not create any fiduciary duties on her part.

# Claims Against Trust

- *3607 Tampico Dr. v. State*, No. 11-13-00306-CV, 2015 Tex. App. LEXIS 13056 (Tex. App.—Eastland Dec. 31, 2015, pet. filed).
- The government brought a forfeiture proceeding under Texas Code of Criminal Procedure Article 59.02(a) for a house owned by a trust.
- The trustee allowed the beneficiary to live in the house while the trust paid for the house and all expenses related to it.
- The beneficiary operated a heroin operation out of the house, and was charged and sentenced to federal prison for that crime.

# Claims Against Trust

- Property that is “contraband” is subject to forfeiture and seizure by the State.
- “Contraband” is property of any nature, including real property, that is used in the commission of the crimes referenced in Article 59.01(2), which includes possession of a controlled substance with intent to deliver.
- After reviewing the evidence, the court held that it supported a reasonable belief that there was a substantial connection between the property and delivery of heroin and that probable cause existed for seizing the property.



# Claims Against Trust

- The court rejected an argument that the state could not seize the property because the perpetrator did not own the property because ownership was not an element.
- Trustee raised an “innocent owner” defense under Chapter 59, and it was her burden to prove that she did not know or should not reasonably have known, at or before the time of acquiring the ownership interest, of the acts giving rise to the forfeiture or that the acts were likely to occur.
- The court of appeals, however, affirmed the trial court’s judgment citing that, at the time the trust purchased the property, the trustee knew that the beneficiary had previously pleaded guilty to possession with intent to distribute nine pounds of marijuana.

# Claims Against Trustee

- *Adams v. Regions Bank*, No. 3:14cv615-DPJ-FKB, 2016 U.S. Dist. LEXIS 1027 (S.D. Miss. Jan. 6, 2016).
- Beneficiaries sued a trustee for multiple claims, including breach of fiduciary duty, arising from the trustee's seizure of collateral owned by the trust.
- Adams, the primary beneficiary, borrowed \$3 million from the bank before it was trustee and signed an agreement pledging the bank's stock as collateral.

# Claims Against Trustees

- Later, the stock was transferred into a testamentary trust created by Adams' father for her benefit.
- Later still, the bank became the trustee of that trust.
- When Adams defaulted on the loan, the bank/trustee proceeded to seize the stock it held in the trust.
- Adams and her children sued the bank for breaching its fiduciary duty in having a conflict of interest and in failing to diversify the trust's assets.
- The bank/trustee filed a motion for summary judgment, which the district court granted

# Claims Against Trustees

- The court first addressed whether Adams' children had standing.
- The trust document provided that Adams was the primary beneficiary, and that she had a power of appointment and could completely cut her children out of the trust.
- Court held that they did not have a present right to the remainder of the trust and did not have standing.

# Claims Against Trustees

- Regarding the non-diversification claims, the court granted the trustee's motion for summary judgment due to a limitations defense.
- The court noted that Adams signed many of the documents that set up the conflict-of-interest situation and participated in litigation to clarify some of those transactions.
- The court held that she did have sufficient information to timely file suit, but did not do so.

# Claims Against Trustees

- The standing issue was very important in this case because the trustee may not have had similar facts to support a limitations defense as against Adams' children, who may have been able to timely raise their claims.
- Under Texas law, the standing decision would be questionable.
- An “interested party” has standing in Texas to bring trust disputes. An interested party includes a “beneficiary.”
- A “Beneficiary” is “a person for whose benefit property is held in trust, regardless of the nature of the interest.”
- “Interest” is “any interest, whether legal or equitable or both, present or future, vested or contingent, defeasible or indefeasible.”

# Claims Against Trustees

- Adams' diversification claim was that the trustee should have sold its own stock and invested in other, better assets.
- Adams' father's will stated that the trustee was "vested with the additional power . . . To retain, with no obligation to sell, any property coming into their hands as Trustees under the terms of this instrument, including stock in AmSouth Bancorp. [now the bank], whether or not the same would be treated as legal for the investment of trust funds and regardless of any lack of diversification or risk, without being liable to any person for such retention unless otherwise specifically provided herein . . . ."
- The court held that the will and a separate retention agreement both allowed the trustee to retain the stock and not diversify until Adams gave written notice to sell the stock.
- As that was never done, the court held that the trustee did not breach its fiduciary duty in keeping the stock in the trust.

# Claims Against Bank Employees

- *Medve v. JPMorgan Chase Bank, N.A.*, No. H-15-2277, 2016 U.S. Dist. LEXIS 11961 (S.D. Tex. Feb. 2, 2016).
- A plaintiff sued a bank and three of its employees for breaches of fiduciary duties arising from fiduciary accounts.
- The bank removed the case to federal court, and the plaintiff filed a motion to remand.
- The issue was whether the plaintiff had pleaded claims against the bank's employees to defeat diversity jurisdiction.



# Claims Against Bank Employees

- The court held that there are three separate legal bases under Texas law for imposing liability on an employee who carries out the fiduciary functions of an entity:
  - (1) “the employee owes a fiduciary duty directly as a subagent carrying out the employer’s fiduciary functions,”
  - (2) “the employee is liable if he ‘participates’ in the employer’s breach of fiduciary duty, which the employee necessarily does if he is the one carrying out the breaches,” and
  - (3) “the employee is personally liable for any tort he commits in the course of his employment, and breach of fiduciary duty is of course a tort.”

# Claims Against Bank Employees

- The plaintiff pleaded that the employees acted as investment advisors and placed the bank's interests above his interests.
- The plaintiff pleaded specific acts of alleged wrongdoing in connection with their rendition of services, including using a fee schedule that favored investments in bank's mutual funds over third party investments that had better rates of return.
- The court held that there was a reasonable basis of recovery for the plaintiff's claims against the employees and remanded the case back to state court.

# No-Contest Clause

- *Ard v. Hudson*, No. 02-13-00198-CV, 2015 Tex. App. LEXIS 8727 (Tex. App.—Fort Worth Aug. 20, 2015, pet. filed).
- A beneficiary sued testamentary trustees and executors for breach of fiduciary duty, sought temporary injunctive relief, and also sought a receiver.
- The trial court granted summary judgment for the defendants on the basis of a no-contest clause.

# No-Contest Clause

- Court of appeals held that a breach of a forfeiture clause will be found only when the beneficiary's or devisee's actions fall clearly within the express terms of the clause.
- Court mentioned other precedent where challenging a fiduciary did not trigger a no-contest clause.
- Defendants agreed with that, but argued that the beneficiary's requests for temporary and permanent injunctive relief and her motions to suspend her brothers as co-trustees and to appoint a receiver triggered the clause.

# No-Contest Clause

- “[The] inherent right [to challenge a fiduciary] would be worthless absent the beneficiary’s corresponding inherent right to seek protection during such an ongoing challenge of what is left of his or her share of the estate or trust assets, and any income thereon, that the testator or grantor, as the case may be, intended the beneficiary to have.”
- Court reversed the summary judgment for the defendants.

# No-Contest Clause

- Defendants also argued that a condition precedent also barred the beneficiary's claims: "Each benefit conferred herein is made on the condition precedent that the beneficiary shall accept and agree to all provisions of this Will."
- Court rejected this argument, holding: "We construe the condition precedent language located within the forfeiture clause to be consistent with the forfeiture clause as a whole."
- Petition for review has been filed.

# Funding of Trust

- *Courtade v. Estrada*, No. 02-14-00295-CV, 2016 Tex. App. LEXIS 3072 (Tex. App.—Fort Worth Mar. 24, 2016, no pet.).
- Estrada created an inter vivos irrevocable trust and deeded real estate into the trust.
- Two days later, Estrada attempted to deed the same property to a daughter.
- After Estrada died, the trustee of her trust and her daughter sued each other regarding the real property and other issues.

# Funding of Trust

- The court held that “It is axiomatic that a grantor cannot convey to a grantee a greater or better title than he holds.”
- The court held: “Although the transcripts reflect that Gloria possibly later changed her mind concerning the rental properties, ‘the deed was already done’-title to the properties had been transferred to the Trust on August 6, 2012.”



# Funding of Trust

- The daughter also alleged that the trust was invalid because Estrada had revoked it.
- The trial court and court of appeals disagreed.
- The document that had the revocation language did not expressly mention the trust, and therefore it was not operative as to the trust.
- Further, the trust stated: “[t]his Trust may not be amended, modified or revoked without the written consent and agreement of the Trustee.”
- As the trustee did not consent in writing to the revocation of the trust, any alleged revocation by the settlor was not effective.

# Funding of Trust

- *In the Estate of Loftis*, No. 07-14-00135-CV, 2015 Tex. App. LEXIS 10940 (Tex. App.—Amarillo Oct. 23, 2015, no pet.).
- A husband and wife entered into a pre-marital agreement.
- After their marriage, they lived in a residence that was the husband's separate property.
- He then executed a will, created a revocable trust, and transferred the residence into the trust.

# Funding of Trust

- The husband filed for divorce but died before the divorce became final.
- The executor/trustee and the wife sued each other regarding the ownership of the residence and other assets.
- The court of appeals held for the wife, and concluded that the pre-marital agreement did control the disposition of the residence as the marriage ended by death and not by divorce.
- However, the court reversed the trial court's order requiring the trustee to deed the residence to the wife as she did not plead for that relief – the court remanded for further proceedings.

# Funding of Trust

- *Dutcher v. Dutcher-Phipps Crane & Rigging, Inc.*, No. 08-15-00202-CV, 2016 Tex. App. LEXIS 3809 (Tex. App.—El Paso Apr. 13, 2016, no pet.).
- A trust owned twenty percent of a family limited partnership that in turn owned a family business.
- The family limited partnership issued shares of the family business to the trustee in his individual name, not in his capacity as trustee.
- After the trustee died, the trustee's wife alleged that the shares went to her under the residuary clause in his will, and that the trust did not own the shares.

# Funding of Trust

- The court of appeals held that a stock certificate “is not synonymous with actual ownership of the shares represented by the certificate; it is merely some evidence of ownership.”
- The court held that establishing ownership depends on the evidence presented, including the nature of the parties, the nature of their relationship, and their representations to each other.
- The court then reviewed the facts and determined that the trustee intended to transfer the stock to himself as trustee, not in his individual capacity.

# Ancillary Remedies

- *Estate of Benson*, No. 04-15-00087-CV, 2015 Tex. App. LEXIS 9477 (Tex. App.—San Antonio Sept. 9, 2015, pet. dismiss'd).
- A beneficiary of a trust sought to remove the trustee, her father, for allegedly violating his fiduciary duties in administering the trust assets.
- News agencies reported that the trustee's current wife was manipulating him, including a claim that she was feeding him mainly candy, ice cream soda, and red wine.
- She also sought and obtained an injunction precluding him from controlling trust assets and also obtained an order appointing co-temporary receivers.

# Ancillary Remedies

- As to the injunction, the court of appeals held that the injunction order was not sufficiently specific and therefore violated the Texas Rules of Civil Procedure.
- The trial court's order merely stated in conclusory fashion that if not granted the beneficiary "would be irreparably harmed," but did not identify any injury that the beneficiary would suffer in the absence of an injunction.
- Harm to trust assets was not sufficient, the court required harm to the applicant/beneficiary.

# Ancillary Remedies

- The court rejected the trustee's challenges to the appointment of temporary co-receivers.
- The court determined that the trial court had some evidence that there was a breach of trust to support its decision to appoint co-receivers.
- Rejecting the trustee's arguments that appointment of co-receivers could not be defended under requirements of equity, the court noted that the beneficiary had sought receivers under Section 114.008(a)(5) of the Texas Property Code, not under equitable grounds.
- Petition for review was filed but has dismissed after settlement of case.



# Standing For Trust Claims

- In *In re XTO Energy Inc.*, No. 05-14-01446-CV, 2015 Tex. App. LEXIS 7723 (Tex. App.—Dallas July 27, 2015, orig. proceeding).
- A beneficiary, on behalf of the trust, sued an oil and gas operator for allegedly not paying sufficient funds to the trust and also sued the trustee for refusing to bring that claim.
- The trustee filed a special exception, requesting that the trial court dismiss the beneficiary's claims as she did not have standing and failed to plead sufficient facts that would allow her to usurp the trustee's authority to determine what legal actions to pursue on behalf of the trust.

# Standing For Trust Claims

- After the trial court denied the special exceptions, the trustee and operator filed a mandamus action.
- The court of appeals first addressed a trustee's authority to control litigation. The court noted that under the Texas Trust Code section 113.019, a trustee is generally authorized to compromise, contest, arbitrate, or settle claims affecting the trust property.
- Further, the terms of trust document may limit or expand trustee powers supplied by the trust code.
- The trust document in the case provided the trustee with discretion to file claims.

# Standing For Trust Claims

- Cases hold that a trust beneficiary may sue on behalf of the trustee “if the trustee cannot or will not do so.”
- The court limited those holdings: “Despite this broad language, a beneficiary may not bring a cause of action on behalf of the trust merely because the trustee has declined to do so. To allow such an action would render the trustee's authority to manage litigation on behalf of the trust illusory.”
- The court “should not allow such a suit to proceed unless the beneficiary pleads and proves that the trustee's refusal to pursue litigation constitutes fraud, misconduct, or a clear abuse of discretion.”

# Standing For Trust Claims

- The court reviewed the underlying claim and held that the trustee's decision, which was based on advice of counsel, was not the result of fraud, misconduct, or a clear abuse of discretion.
- The court held that the beneficiary improperly sued the trustee *on behalf of the trust* because only the trustee can do that.
- The court held, however, that The Texas Trust Code allows a beneficiary to sue a trustee *on her own behalf* regarding the trustee's decision to not sue the operator.
- Plaintiff was allowed to replead this aspect of her claim.

# Claims By Trustee

- *Estate of Sloan*, No. 02-15-00198-CV, 2016 Tex. App. LEXIS 6465 (Tex. App.—Fort Worth June 16, 2016, no pet. history).
- A wife died leaving her home, and her husband was the executor of her estate and trustee of testamentary trusts.
- The wife's will left all of her assets to three trusts, but provided that her husband could buy assets for fair market value.
- The husband traded rental properties for the wife's home for half of its value (asserting community property interest).

# Claims By Trustee

- The trustee sued husband's estate for breach of fiduciary duty, claiming that the property was the wife's separate property and that the husband underpaid for the house by only paying for half.
- The trial court ruled for the trustee, and the husband's estate appealed.
- A "property's fair market value is what a willing buyer would pay a willing seller, neither acting under any compulsion."
- Texas Constitution article XVI, section 52 provides that a surviving spouse may occupy the homestead during the spouse's lifetime without it being partitioned to the heirs of the deceased spouse until the survivor's death.

# Claims By Trustee

- Because the parties stipulated that if the husband's interest decreased the value of the property, his estate would not owe anything, the court of appeals reversed and rendered for his estate because the homestead interest did decrease the value.
- The court also concluded: "In light of our holding above that Hollis's homestead right decreased the fair market value of the estate's interest in the property, of the trial court's uncontested finding that Hollis was entitled to \$25,000 in community reimbursement when he bought the property, and of the explicit authorization in Barbara's will for Hollis to purchase assets from her estate at fair market value, we cannot conclude that Hollis violated fiduciary duties when buying the Winton Terrace Property."
- Court held this despite the fact that husband never disclosed the transaction to any beneficiary during his life.

# Bankruptcy Issues

- *Archer v. Allison*, No. 07-14-003130CV, 2015 Tex. App. LEXIS 12361 (Tex. App.—Amarillo Dec. 3, 2015, pet. denied).
- A plaintiff sued his daughter and her husband for breaching fiduciary duties and other similar causes of action related to their work in certain businesses.
- The plaintiff had previously represented to a bankruptcy court in 2002 that he had no interest in the properties at issue.
- The defendants filed motions for summary judgment based on judicial estoppel, which the trial court granted.



# Bankruptcy Issues

- Judicial estoppel is a common law principle that applies when a party contradicts his sworn statement in prior litigation.
- The affirmative defense is established through proof that 1) the positions were clearly inconsistent, 2) the court in the prior proceeding accepted the position, and 3) the prior position was asserted intentionally rather than inadvertently.
- The court explained: “Simply put, Archer previously represented in a legal proceeding that he claimed no interest in various of properties he now attempts to recoup.”

# Bankruptcy Issues

- Section 523(a)(4) of the Federal Bankruptcy Code provides that an individual cannot obtain a bankruptcy discharge from a debt “for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.” 11 U.S.C. §523(a)(4).
- A defalcation must involve either (i) moral turpitude, bad faith, or other immoral conduct, or (ii) in lieu of these, an intentional wrong, which includes not only conduct that the fiduciary knows is improper but also reckless conduct of the kind that the criminal law often treats as the equivalent, such as where the fiduciary consciously disregards, or is willfully blind to, a substantial and unjustifiable risk that his conduct will turn out to violate a fiduciary duty. *Bullock v. BankChampaign, N.A.*, 133 S.Ct. 1754, 1759, 185 L.Ed.2d 922 (2013).

# Bankruptcy Issues

- In an adversary proceeding under § 523(a)(4), a bankruptcy court may apply collateral estoppel "to preclude relitigation of state court findings that are relevant to dischargeability." *Whitaker v. Moroney Farms Homeowners' Ass'n (In re Whitaker)*, No. 15-40926, 2016 U.S. App. LEXIS 5018 (5th Cir. Mar. 18, 2016).
- Where the state court judgment has sufficient findings of fact that support a finding of defalcation, a bankruptcy court may apply collateral estoppel and deny the discharge of the debt.

# Bankruptcy Issues

- *Smith v. Saden*, No. 10-35051, 2016 Bankr. LEXIS 877 (S.D. Tex. Bankr. Mar. 7, 2016).
- A plaintiff obtained a judgment against a defendant, which included a disgorgement award based on a breach of fiduciary duty.
- The plaintiff failed to plead or submit a jury question on whether the defendant committed acts of fraud, defalcation, and embezzlement.
- The court then noted that the plaintiff needed to request a trial in the bankruptcy court on whether any amounts should be excepted from discharge due to the breach-of-fiduciary-duty disgorgement.

# Tortious Interference Claim

- *Anderson v. Archer*, No. 03-13-00790-CV, 2016 Tex. App. LEXIS 2165 (Tex. App.—Austin Mar. 2, 2016, no pet.).
- The trial court's judgment awarded the plaintiffs \$2.5 million in damages based on a tortious interference with inheritance claim.
- The defendants appealed and argued that Texas law does not recognize such a claim.

# Tortious Interference Claim

- The court of appeals cited with agreement to a recent opinion from the Amarillo court of appeals that held that Texas has not adopted a tortious interference with inheritance claim: *Jackson Walker, LLP v. Kinsel*, No. 07-13-00130-CV, 2015 Tex. App. LEXIS 3586 (Tex. App.—Amarillo Apr. 10, 2015, pet. filed).
- Court held that it was not a subset of the tort of tortious interference with a contract or prospective contractual or business relationship, and held that it was a separate claim that had not yet been recognized.

# Exemplary Damages

- *Davis v. White*, No. 02-13-00191-CV, 2016 Tex. App. LEXIS 3075 (Tex. App.—Fort Worth Mar. 24, 2016, no pet.).
- A lawyer sued his former partner over the application of a receivable, and the jury awarded the plaintiff damages and exemplary damages.
- The trial court awarded the plaintiff his actual damages, but applied the exemplary damages cap, and limited that award to around \$550,000.

# Exemplary Damages

- The plaintiff appealed, arguing that the cap should not have been applied because he pleaded and proved that the defendant's actions fell within the "misapplication of fiduciary property" exception to the cap listed in Texas Civil Practice and Remedies Code section 41.008(c)(10).
- The court of appeals disagreed, holding that the plaintiff did not plead facts in support of the capbuster "in relation to his punitive damages claim."



# Slayer Rule

- *Estate of Huffines*, No. 02-15-00293-CV, 2016 Tex. App. LEXIS 4469 (Tex. App.—Fort Worth April 28, 2016, no pet. history).
- A wife and husband opened accounts that were JTROS, and then the husband killed the wife and committed suicide.
- The executors of their estates fought over who owned the money in the accounts.

# Slayer Rule

- The wife's estate claimed that the entire amount in the accounts should go to it because of the Slayer Rule and also because the money was allegedly the wife's separate property.
- The wife's estate brought claims against the bank for disbursing only half of the money to it and freezing the rest pending a court order.
- The trial court eventually entered an order for the bank, and the wife's estate appealed.

# Slayer Rule

- The court of appeals held that there was a fact question as to whether the funds were separate or community property.
- The court stated that Texas law generally provides that a husband or wife who murders his or her spouse may not inherit under the spouse's will as a beneficiary.
- But the court also held that an heir must plead for the imposition of a constructive trust over the property to be inherited by the murderer.
- As that was not done in this case, the bank acted reasonably in not releasing the funds absent a court order.

# 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.