

Remedies For Breach Of Fiduciary Duty Claims

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Introduction

- A fiduciary owes its principal one of the highest duties known to law—this is a very special relationship.
- Fiduciary duties can arise in many different formal relationships, such as trustee/beneficiary, partners, lawyer/client, and joint venturers.
- In addition, certain informal relationships can give rise to a fiduciary duty, “where one person trusts in and relies upon another, whether the relation is a moral, social, domestic or merely personal one.”

Introduction

- Due to the special nature of the fiduciary relationship, there is likely no area of law that has such a wide range of remedies available to a plaintiff than in breach-of-fiduciary-duty cases.
- A plaintiff may obtain a plethora of both legal and equitable remedies.
- This presentation is intended to provide general guidance on the available remedies for breach-of-fiduciary-duty claims.

Pre-Trial Remedies

- A plaintiff often needs to seek a remedy before trial to protect it from immediate injury, to protect the assets made the basis of the suit, or to discover the real condition of the parties' relationship.
- We are going to discuss three pre-trial remedies that are potentially available to a plaintiff: temporary injunctive relief, receiverships, and audits.

Temporary Injunctions

- A plaintiff may need to seek immediate relief from a court to prevent a fiduciary from selling assets, using assets, or failing to distribute assets to the plaintiff.
- The common law and Texas statutes provide authority for temporary injunctive relief. Texas Civil Practice and Remedies Code section 65.011 authorizes injunctive relief.
- Moreover, specific statutes may apply to fiduciaries. For example, Texas Trust Code Section 114.008(2) provides for injunctive relief as a remedy for breach of trust that “has occurred or may occur.” Tex. Prop. Code § 114.008(2).

Temporary Injunctions

- To show a probable right of recovery, an applicant need not establish that it will finally prevail in the litigation; rather, it must only present some evidence that, under the applicable rules of law, tends to support its cause of action.
- In a fiduciary case, there is authority that the usual burden of establishing a probable right of recovery does not apply if the gist of the complaint is that a fiduciary is guilty of self-dealing.
- There is a presumption of unfairness.

Temporary Injunctions

- Irreparable injury must be imminent and not speculative.
- Evidence that a defendant may continue to divert fiduciary funds may be sufficient.
- There is authority that there is no irreparable-injury requirement when the defendant is a fiduciary.

Receiverships

- A plaintiff may wish to seek a receivership to have an independent third party manage assets pending the resolution of the plaintiff's claims.
- There are multiple statutes in Texas that allow for receivership relief. The most used statute allowing for receiverships is Texas Civil Practice and Remedies Code Chapter 64 that allows receiverships in specified types of cases and when permitted by the usages of equity. Tex. Civ. Prac. & Rem. Code § 64.001 et seq.
- There are other statutes that allow receiverships in various areas of law: there are statutes that allow receiverships for business entities (Tex. Bus. Orgs. Code § 11.403 et seq.), religious congregations (Tex. Civ. Prac. & Rem. Code § 126.001 et seq.), insurers (Tex. Ins. Code Art. 21.28), family law situations (Tex. Fam. Code § § 6.502(5), 6.709(3)), mineral interests (Tex. Civ. Prac. & Rem. Code § § 64.091, 64.092), and trusts (Tex. Prop. Code § 114.008).

Receiverships

- “Chapter 64 of the Civil Practice and Remedies Code sets forth the circumstances under which a trial court may appoint a receiver.”
- A court of competent jurisdiction may appoint a receiver: (1) in an action by a vendor to vacate a fraudulent purchase of property; (2) in an action by a creditor to subject any property or fund to his claim; (3) in an action between partners or others jointly owning or interested in any property or fund; (4) in an action by a mortgagee for the foreclosure of the mortgage and sale of the mortgaged property; (5) for a corporation that is insolvent, is in imminent danger of insolvency, has been dissolved, or has forfeited its corporate rights; or (6) in any other case in which a receiver may be appointed under the rules of equity.
- Under Subsection (a)(1), (2), or (3), the party must have a probable interest in or right to the property or fund, and the property or fund must be in danger of being lost, removed, or materially injured.

Receiverships

- Texas Trust Code Section 114.008 provides for receivership relief as a remedy for breach of trust that “has occurred or may occur.” Tex. Prop. Code § 114.008.
- Are other equitable requirements necessary?
- Trust cases: *Estate of Benson*, No. 04-15-00087-CV, 2015 Tex. App. LEXIS 9477 (Tex. App.—San Antonio Sept. 9, 2015, pet. dismiss. by agr.); *Elliott v. Weatherman*, 396 S.W.3d 224, 228 (Tex. App.—Austin 2013, no pet.).

Audits

- A plaintiff may want an independent third party to provide an accounting of the fiduciary relationship before trial.
- Texas Rule of Civil Procedure 172 allows a court to appoint an auditor to state the accounts between the parties and to make a report thereof to the court. Rule 172 states:
- “When an investigation of accounts or examination of vouchers appears necessary for the purpose of justice between the parties to any suit, the court shall appoint an auditor or auditors to state the accounts between the parties and to make report thereof to the court as soon as possible.”

Audits

- “The auditor shall verify his report by his affidavit stating that he has carefully examined the state of the account between the parties, and that his report contains a true statement thereof, so far as the same has come within his knowledge. Exceptions to such report or of any item thereof must be filed within 30 days of the filing of such report. The court shall award reasonable compensation to such auditor to be taxed as costs of suit.”
- “The purpose of the appointment is to have an account so made up that the undisputed items upon either side may be eliminated from the contest, and the issues thereby narrowed to the points actually in dispute.”

Other Pre-Trial Remedies

- In addition, a party should consider other potential pre-trial remedies, such as:
- Attachment;
- Sequestration;
- Garnishment; and
- Repossession.

Legal Remedies

- A plaintiff may be awarded legal remedies, such as damages.
- A plaintiff may be awarded his or her actual damages for breach of fiduciary duty and include both general/direct damages and special/consequential damages.

Legal Remedies: Direct Damages

- “Direct damages,” also known as “general damages,” are those inherent in the nature of the breach of the obligation between the parties, and they compensate a plaintiff for a loss that is conclusively presumed to have been foreseen by the defendant as a usual and necessary consequence of the defendant’s act.
- “Benefit of the bargain” measure utilizes an expectancy theory and evaluates the difference between the value as represented and the value received.

Legal Remedies: Lost Profits

- Lost profits are recoverable for a breach-of-fiduciary-duty claim.
- Lost profits may be in the form of direct damages, that is, profits lost on the contract itself, or in the form of consequential damages, such as profits lost on other contracts or relationships resulting from the breach.

Legal Remedies: Lost Profits

- Recovery for lost profits does not require that the loss be susceptible of exact calculation.
- However, the injured party must do more than show that they suffered some lost profits.
- The amount of the loss must be shown by competent evidence with reasonable certainty.
- Estimates of lost profits must be based on objective facts, figures, or data from which the amount of lost profits can be ascertained.
- The plaintiff bears the burden of providing evidence supporting a single complete calculation of lost profits, which may often require certain credits and expenses.

Legal Remedies: Mental Anguish

- One particular subset of actual damages is mental anguish and/or emotional distress damages if the damages are a foreseeable result of a breach of fiduciary duty.
- For example, an attorney breached his fiduciary duty by disclosing a client's confidential information to a district attorney and an allegation of emotional distress constituted sufficient damage to sustain the claim.

Legal Remedies: Mental Anguish

- Intentional conduct necessary for recovery of mental anguish in attorney malpractice cases.
- “The term ‘mental anguish’ implies a relatively high degree of mental pain and distress. It is more than mere disappointment, anger, resentment or embarrassment, although it may include all of these. It includes a mental sensation of pain resulting from such painful emotions as grief, severe disappointment, indignation, wounded pride, shame, despair and/or public humiliation.”
- An award for mental anguish will normally survive appellate review if “the plaintiffs have introduced direct evidence of the nature, duration, and severity of their mental anguish thus establishing a substantial disruption in the plaintiff’s routine.”

Legal Remedies: Mental Anguish

- *Martin v. Martin*, the court of appeals reversed a mental anguish award against a trustee based on a claim of intentional breach of fiduciary duty because the beneficiary did not have sufficient evidence of harm. 363 S.W.3d 221 (Tex. App.—Texarkana 2012, pet. denied).
- *Wells Fargo v. Militello*, a court affirmed a mental anguish award against a trustee. No. 05-15-01252-CV, 2017 Tex. App. LEXIS 5640 (Tex. App.—Dallas June 20, 2017, pet. denied).

Legal Remedies: Out of Pocket

- In addition, a plaintiff may be entitled to out-of-pocket damages.
- The out-of-pocket measure of damages requires a court to consider the difference between the value paid and the value received.
- The out-of-pocket measure compensates only for actual injuries a party sustains through parting with something, not loss of profits not yet realized.

Legal Remedies: Consequential Damages

- A plaintiff may also be entitled to award consequential damages.
- Consequential damages are defined as “those damages which result naturally, but not necessarily, from the defendant’s wrongful acts.”
- Can be lost profits for other contracts.
- Expenses in remedying the breach. *Wells Fargo v. Militello*, No. 05-15-01252-CV, 2017 Tex. App. LEXIS 5640 (Tex. App.—Dallas June 20, 2017, pet. denied).

Legal Remedies: Attorney's Fees

- Attorney's fees are not recoverable unless authorized by statute or provided for by contract.
- First, there are specific statutes that may allow an award of attorney's fees in breach of fiduciary duty disputes, such as trust disputes. Tex. Prop. Code Ann. § 114.064.
- Second, a party can seek an award of attorney's fees as damages, i.e., where the defendant's conduct has caused the plaintiff to incur attorney's fees in a separate suit.
- Common-fund theory.
- A plaintiff may be entitled to an award of pre-judgment interest, but it is generally discretionary with the court.

Legal Remedies: Punitive Damages

- A plaintiff may also be entitled to an award of punitive damages.
- A jury may only award exemplary damages if the claimant proves, by clear and convincing evidence, that the harm resulted from: (1) fraud; (2) malice; or (3) gross negligence. Tex. Civ. Prac. & Rem. Code Ann. § 41.003(a).
- “Exemplary damages may be awarded only if the jury was unanimous in regard to finding liability for and the amount of exemplary damages.” *Id.* at § 41.003(d).

Legal Remedies: Punitive Damages

- “Fraud” means fraud other than constructive fraud. Tex. Civ. Prac. & Rem. Code § 41.001(6).
- “Malice” means a specific intent by the defendant to cause substantial injury or harm to the claimant. *Id.* at 41.001(7).
- “Gross negligence” means an act or omission: (A) which when viewed objectively from the standpoint of the actor at the time of its occurrence involves an extreme degree of risk, considering the probability and magnitude of the potential harm to others; and (B) of which the actor has actual, subjective awareness of the risk involved, but nevertheless proceeds with conscious indifference to the rights, safety, or welfare of others. *Id.* 41.001(11).

Legal Remedies: Punitive Damages

- One important protection for defendants is the statutory cap on the amount of exemplary damages.
- The Texas Civil Practice and Remedies Code permits exemplary damages of up to the greater of: (1) (a) two times the amount of economic damages; plus (b) an amount equal to any noneconomic damages found by the jury, not to exceed \$750,000; or (2) \$200,000. Tex. Civ. Prac. & Rem. Code Ann. § 41.008(b).

Legal Remedies: Punitive Damages

- “Economic damages” means compensatory damages intended to compensate a claimant for actual economic or pecuniary loss; the term does not include exemplary damages or noneconomic damages. Tex. Civ. Prac. & Rem. Code § 41.001(4).
- “Noneconomic damages” means damages awarded for the purpose of compensating a claimant for physical pain and suffering, mental or emotional pain or anguish, loss of consortium, disfigurement, physical impairment, loss of companionship and society, inconvenience, loss of enjoyment of life, injury to reputation, and all other nonpecuniary losses of any kind other than exemplary damages. *Id.* 41.001(12).

Legal Remedies: Punitive Damages

- These limits do not apply to claims supporting misapplication of fiduciary property or theft of a third-degree felony level. Tex. Civ. Prac. & Rem. Code Ann. § 41.008(c)(10).
- The caps “do not apply to a cause of action against a defendant from whom a plaintiff seeks recovery of exemplary damages based on conduct described as a felony in the following sections of the Penal Code if ... the conduct was committed knowingly or intentionally....” *Id.*
- Accordingly, if a defendant is found liable for one of these crimes with the required knowledge or intent, it cannot take advantage of the statutory exemplary damages caps.

Legal Remedies: Punitive Damages

- A person commits the offense of misapplication of fiduciary property by intentionally, knowingly, or recklessly misapplying property he holds as a fiduciary in a manner that involves substantial risk of loss to the owner of the property. Tex. Pen. Code § 32.45(b).
- “Substantial risk of loss” means a real possibility of loss; the possibility need not rise to the level of a substantial certainty, but the risk of loss does have to be at least more likely than not.
- Need a jury finding?

Equitable Remedies

- A fiduciary relationship is based in equity.
- Therefore, a court may award equitable remedies for breach of fiduciary duty.
- A trial court may order that the fiduciary forfeit compensation otherwise earned, disgorge improper gains and profits, or disgorge other consideration related to the breach of duty.

Equitable Remedies: Compensation Forfeiture

- Under the equitable remedy of forfeiture, a person who renders service to another in a relationship of trust may be denied compensation for her service if he breaches that trust.
- The objective of the remedy is to return to the principal the value of what the principal paid because the principal did not receive the trust or loyalty from the other party.

Equitable Remedies: Compensation Forfeiture

- Where equitable remedies exist, “the remedy of forfeiture must fit the circumstances presented.”
- There are several factors for consideration when fashioning a particular equitable-forfeiture remedy: “[T]he gravity and timing of the violation, its willfulness, its effect on the value of the lawyer’s work for the client, any other threatened or actual harm to the client, and the adequacy of other remedies.”
- These factors are to be considered in determining whether a violation is clear and serious, whether forfeiture of any fee should be required, and if so, what amount.
- The list is not exclusive.

Equitable Remedies: Compensation Forfeiture

- In exercising its discretion, a court should consider the following factors: (1) whether the trustee acted in good faith or not; (2) whether the breach of trust was intentional or negligent or without fault; (3) whether the breach of trust related to the management of the whole trust or related only to a part of the trust property; (4) whether or not the breach of trust occasioned any loss and whether if there has been a loss it has been made good by the trustee; and (5) whether the trustee's services were of value to the trust.

Equitable Remedies: Compensation Forfeiture

- The trial court should make that determination under the multiple-factor test based on the evidence in the case.
- The trial court can rule that the defendant should forfeit some, all, or none of the compensation.
- The remedy of forfeiture for a fiduciary's breach is dependent upon the facts and circumstances in each case.

Equitable Remedies: Profit Disgorgement

- Disgorgement of profits or benefits is an equitable remedy appropriate when a party has breached his fiduciary duty; its purpose is to protect relationships of trust by discouraging disloyalty.
- Disgorgement of profits requires the fiduciary to yield to the beneficiary the profit or benefit gained during the time of the breach.
- Disgorgement is distinct from an award of actual damages in that the disgorgement award serves a separate function of deterring fiduciaries from exploiting their positions of confidence and trust.

Equitable Remedies: Profit Disgorgement

- “Disgorgement is compensatory in the same sense attorney fees, interest, and costs are, but it is not damages.”
- Disgorgement of profits requires the fiduciary to yield to the beneficiary the profit or benefit gained during the time of the breach.
- The fiduciary only has to disgorge “profits” and does not have to disgorge net revenues. *Longview Energy Co. v. Huff Energy Fund LP*, No. 15-0968, 2017 Tex. LEXIS 525 (Tex. June 9, 2017).

Equitable Remedies: Profit Disgorgement

- It should also be noted that the trial court should order a fiduciary defendant to disgorge all improper profits, and there does not have to be a weighing of factors to determine whether and how much should be disgorged as there does in compensation forfeiture cases.

Equitable Remedies: Consideration Disgorgement

- A plaintiff can potentially seek the disgorgement of contractual consideration from a defendant.
- *ERI Consulting Eng'rs, Inc. v. Swinnea*, 318 S.W.3d 867 (Tex. 2010).
- Court remanded for a determination of whether the forfeiture factors supported the trial court's award.
- The court of appeals affirmed that award after reviewing the factors.

Equitable Remedies: Consideration Disgorgement

- *Cooper v. Sanders H. Campbell/Richard T. Mullen, Inc.*, No. 05-15-00340-CV, 2016 Tex. App. LEXIS 9253 (Tex. App.—Dallas August 24, 2016, no pet.).
- The court of appeals held that the record did not support the trial court's award, and remanded the case for further proceedings to allow the trial court to consider the appropriate legal standards, elements, and factors in awarding a forfeiture remedy.

Other Potential Remedies

- Removal of Fiduciary
- Constructive Trust
- Accounting
- Permanent Injunction
- Rescission
- Equitable Lien
- Declaratory Relief
- Partition

Determination of Remedy

- Is a plaintiff or defendant entitled to submit a requested remedy, or any aspect of it, to a jury or may a trial court alone determine the availability of the remedy?
- If requested, a jury should determine the amount of damages at law that should be awarded to a plaintiff where there is a fact issue.
- A court, in its equitable jurisdiction, should determine whether an equitable remedy should be granted.

Determination of Remedy

- If properly requested and preserved, a party is entitled to submit a fact issue on legal damages to a jury.
- However, if a party seeks an equitable remedy, the trial court normally has the sole right to resolve that request.
- If there is some underlying fact issue that must be resolved with regard to the equitable remedy, then that fact issue should be submitted to a jury.
- Parties should be very careful to evaluate all requested remedies before trial and determine what should be submitted to the court and what should be submitted to a jury.
- Otherwise, after trial, a court may determine that a party waived the right to a jury on a fact issue, and either refuse to award the remedy or grant the remedy and with supporting findings found in favor of the judgment.

Widening The Net

- A hot topic in the past year is the use and confines of net widening theories such as knowing participation, aiding and abetting, and conspiracy to commit a breach of fiduciary duty.
- Damages for same only applies after the defendant joins the conspiracy—complex causation issues now arise.

Conclusion

- There is no area of the law where remedies abound more than in fiduciary claims.
- This requires attorneys to be very creative in seeking and defending against those remedies.
- The author hopes that this presentation assists in that analysis.