



# **FISHING WITHOUT A HOOK:**

## **FIDUCIARY LIABILITY IN THE AGE OF DIRECTED TRUSTS, INDEMNIFICATION AND EXONERATION**

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# OVERVIEW OF LIMITATIONS TO FIDUCIARY LIABILITY

- National movement in the area of trust law over the past two decades to limit fiduciary liability in context of trust administration and litigation.
- Laws permitting the drafting of expansive exoneration and exculpation clauses in trust instruments.
- Laws permitting the waiver of statutory and common law duties.

# OVERVIEW OF LIMITATIONS TO FIDUCIARY LIABILITY

- Implementation of trust protector statutes.
- Rise of directed trust statutes.
- The fine tuning of trust protector statutes and directed trust statutes:
  - Limiting or eliminating the fiduciary relationship for directors/advisers;
  - Limitation or complete exoneration of liability for directed fiduciaries following directives of directors.

JUST BECAUSE THE HOOKS ARE BEING TAKEN AWAY, DOES  
NOT MEAN YOU CANNOT BE CAUGHT



# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Limitations or deviations permitted within the trust instrument:
  - NRS 163.004 permits the trust instrument to limit the rights of beneficiaries, in any manner, including limitations on rights to sue:
    - Cannot be illegal or against public policy (NRS 163.004(1)); and
    - Cannot authorize exculpation or indemnification of fiduciary for its own willful misconduct or gross negligence (NRS 163.004(3)(a)).

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Limitations or deviations permitted within the trust instrument (cont'd):
  - NRS 163.160 permits the trust instrument to relieve and alter duties, restrictions, liabilities, or to add privileges or powers of a trustee:
    - Cannot relieve trustee of liability for breach of trust committed with gross negligence, intentional misconduct, bad faith or reckless indifference to interest of beneficiary (NRS 163.160.(3)(a)); and
    - Cannot relieve trustee of liability for profit that trustee derives from a breach of trust (NRS 163.160(3)(b).

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Limitations or deviations permitted within the trust instrument (cont'd):

Corollary to NRS 163.160:

- NRS 163.130 expressly permits exoneration of trustee for tort:
  - where the trust instrument authorizes exoneration or reimbursement: and
  - the actions did not constitute willful misconduct or gross negligence.



# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Limitations or deviations permitted within the trust instrument (cont'd):
- Corollary to NRS 163.160:
  - NRS 163.130 expressly permits exoneration of trustee for tort:
    - where the trust instrument authorizes exoneration or reimbursement: and
    - the actions did not constitute willful misconduct or gross negligence.



# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Exoneration permitted by beneficiary during administration of the trust:
  - NRS 163.170. Beneficiary may relieve a trustee of any or all of the duties, restrictions and liabilities that would otherwise be imposed on the trustee if:
    - if possessing legal capacity; and
    - acting on “full information”

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Exculpation or exoneration permitted by court during administration of the trust:
- NRS 163.180:
  - Court may relieve a trustee from any duty or restriction imposed under Nevada law
    - For cause shown and with notice to beneficiaries
  - Court may excuse a trustee for an action/failure to act
    - If trustee has acted honestly and reasonably.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Trusts-- Types of Advisers
  - 163.5536: “Directing Trust Adviser” means a trust adviser, trust protector or other who has authority under trust to give directions that MUST be followed by the fiduciary.
    - NOTE: more than just recommendations, has authority to direct the fiduciary.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Trusts-- Types of Advisers (cont'd)
  - NRS 163.5545: "Trust Adviser" means distribution trust adviser or investment trust adviser.
  - NRS 163.5537: "Distribution Trust Adviser" is a fiduciary who has authority under trust to exercise powers/direction under NRS 163.5557(3)
    - Distribution powers in its sole discretion must be exercised in "the best interest of the trust."

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Trusts-- Types of Advisers (cont'd)
  - NRS 163.5543: "Investment Trust Adviser" a fiduciary who has authority to exercise powers/direction under NRS 163.5557(2):
    - provided investment powers in his sole discretion that must be exercised in "the best interest of the trust."
    - Includes specific powers to:
      - Direct trustee regarding retention, sale, purchase or encumbrance of property;
      - Vote proxies for securities;
      - Select investment advisers and delegate powers of investment trust adviser.
  - NOTE: Distinguish 163.275(2), which permits fiduciary to delegate investment authority, but does not relieve liability existing in absence of delegation.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Trusts-- Types of Advisers (cont'd)
  - NRS 163.5547: "Trust Protector" is person who is appointed in such capacity under the trust.
  - NRS 163.5553: Trust may include powers exercised in sole discretion such as:
    - Amend trust for tax status or changes in law;
    - Amend trust to take advantage in changes to perpetuities periods, restraints on alienation or other laws restricting terms of the trust;
    - Increase/decrease interests of beneficiary;
    - Modify terms of power of appointment but cannot grant beneficial interest to person not specifically provided for in trust instrument;

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Trusts-- Types of Advisers (cont'd):

- NRS 163.5553: Powers (continued):

- Terminate the trust;
    - Remove/appoint trustee, trust adviser, investment committee members, distribution committee members;
    - Direct/veto trust distributions;
    - Change location of governing law;
    - Interpret terms of instrument;
    - Advise trustee on beneficiary matters; and
    - Review/approve trustee's reports or accounting.



# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Liability of Advisers:

- NRS 163.5551: trust advisers are considered fiduciaries if they are given authority to direct a fiduciary's investment decisions unless instrument provides otherwise.
- NRS 163.554: fiduciary includes trustee, investment trust adviser, trust protector, trust committee acting in fiduciary capacity.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Directed Fiduciaries:

- NRS 163.5548: Directed fiduciary is a fiduciary who:
  - Has no power to take under the terms of the instrument
  - Is mandated by trust and has no discretion to act in derogation
  - Is directed by a directing trust adviser.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Liability of Directed Fiduciaries:

- NRS 163.5549: Limitation on liability of directed fiduciaries
  - No duty to perform suitability review, inquire, investigate or make any recommendation regarding any investment if investment is made by directing trust adviser.
  - No liability for loss resulting from
    - complying with direction of directing trust adviser; or
    - failing to act on such direction if requiring approval/consent of another person (which has not been provided) or is contingent on an unsatisfied condition.

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Restatement of Law (3d) Trusts Section 75: Likely catchall in absence of express statutory exoneration.
  - “If the terms of a trust reserve to the settlor or confer upon another a power to direct or otherwise control certain conduct of the trustee, the trustee has a **DUTY** to act in accordance with the requirements of the trust provision ... and to comply with any exercise of that power, unless the attempted exercise is contrary to the terms of the trust or power or the trustee knows or has reason to believe that the attempted exercise violates a fiduciary duty that the power holder owes to the beneficiaries.”

# OVERVIEW OF NEVADA'S FIDUCIARY LIABILITY LIMITATIONS

- Restatement of Law (3d) Trusts Section 75: Likely catchall in absence of express statutory exoneration (cont'd).
  - Key distinction of Section 75, requires trustee to analyze the directive:
    - No exoneration if the attempted exercise is contrary to the terms of the trust or power.
    - No exoneration if trustee knows or has reason to believe that the attempted exercise violates a fiduciary duty that the power holder owes to the beneficiaries.”

# EXONERATION IN ACTION

- Nevada has no reported case law that discusses the scope or extent of a trustee's exoneration.
- Exemplar cases from other jurisdictions provide some guidance.

# EXONERATION IN ACTION

- *Duemler v. Wilmington Trust Co.*, 2004 WL 5383927 (Del.Ch.):
  - Trustee subject to investment adviser not liable to beneficiary (who was the investment adviser) for failure to provide investment information.
  - Court relies upon analogous Delaware statute (12 Del.C 3313(b)) for insulation of liability for directed fiduciaries.
  - Alternatively found beneficiary had actual knowledge of the investment information so any failure to provide information was not the proximate cause of the loss.



# EXONERATION IN ACTION

- *Rollins v. Branch Banking and Trust Company of Virginia*, 2001 WL 34037931 (Va.Cir.Ct.):
  - Corporate trustee was directed trustee and not liable for claim for failure to diversify trust investments where trust instrument required investment decisions to be determined by the adult beneficiaries.
  - “The [Virginia statute] recognizes the basic principle that the court cannot hold a trustee or anyone else, liable for decisions that it did not and could not have made.”

# EXONERATION IN ACTION

- *Friedman v. U.S. Trust Company of Delaware, C.A., No. 20205 NC (2003 Del.Ch.)*:
  - Corporate trustee whose powers were essentially relegated to those of an administrative trustee not liable for transactions that removed settlor's control over entities held by the trust where settlor's son was trust protector who possessed virtually all powers of a traditional trustee.

# EXONERATION IN ACTION

- *Rogers v. Wilmington Trust Co.*, 2022 WL 621690 (3rd Cir. 2022)
  - Where neither Delaware law nor provision of trust prohibited trustee from also serving as an investment trust adviser, trustee could serve in both capacities did not breach fiduciary duty to avoid conflicts of interest.

## EXONERATION IN ACTION (HONORABLE MENTION FOR CREATIVITY)

- *Paradee v. Paradee*, 2010 WL 3959604 (Del.Ch. 2010)
  - Trust contained provision exonerating trustee for reliance on advice of counsel.
  - Court analyzed exoneration provision for advice of counsel, as being analogous to a directed trustee under 12 Del.C. 3313(b).
  - Court found as a factual matter that trustee still liable because did not follow the advice of the attorney.

# TAKING LIMITATIONS OF LIABILITY TO THE EXTREME

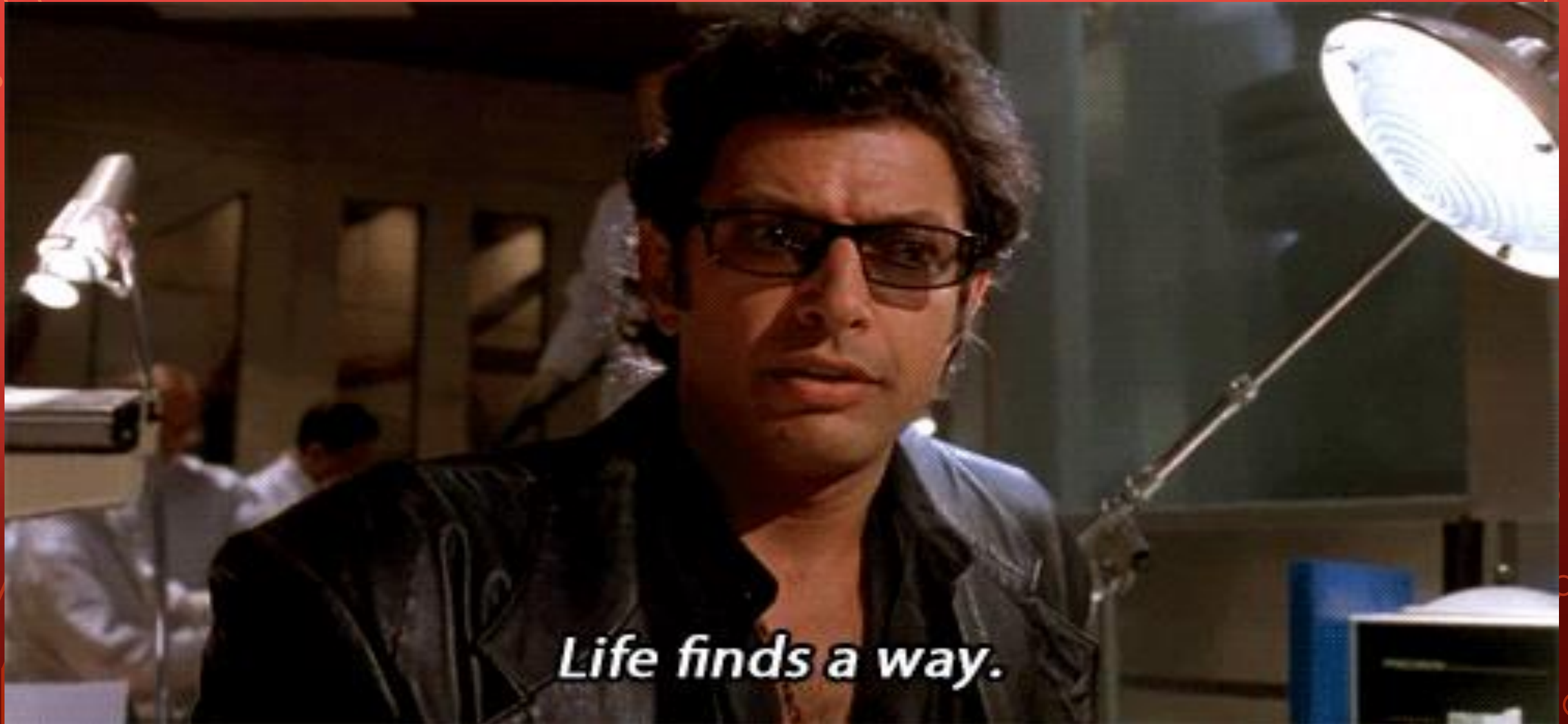
- The limitations on liability, statutory exonerations and emergence of persons with no fiduciary duty directing fiduciaries, have led some to surmise that it is conceptually possible to create a non-fiduciary trust, essentially disregarding “irreducible core” concepts of a trust:
  - The beneficiary must be able to enforce certain duties owed him or her by the trustee;
  - While the default fiduciary duties owed by the trustee to the beneficiary may be waived by the trust instrument, there must be at least some duties owed by the trustee to the beneficiary;
  - The trustee must act in good faith and not in bad faith or with willful misconduct; and
  - The trustee must be held liable to the beneficiaries when the trustee acts in bad faith or with willful misconduct.

# TAKING LIMITATIONS OF LIABILITY TO THE EXTREME

- “It does appear that it is now possible to fashion a nonfiduciary trust, one in which no fiduciary duties are owed to the beneficiaries by either the trustee or directors, so that there are no interests that the beneficiaries are able or even entitled to defend, or, alternatively, of which the beneficiaries may have absolutely no knowledge or insufficient knowledge so as to defend their interests meaningfully.”

- Schoenblum, Jeffrey (2021) “The Nonfiduciary ‘Trust’,” ACTEC Law Journal: Vol. 46; No. 3, Article 4.

# LIFE (LIKE LIABILITY) FINDS A WAY





## POTENTIAL HOOKS FOR LIABILITY

- “‘Equity will not suffer a wrong to be without a remedy’ is a maxim of equity which has long been invoked and universally applied.”
  - *Seaborn v. First Judicial District Court*, 55 Nev. 206, 29 P.2d 500, 505 (1934).
- Courts of equity have the power, where necessary, to pierce rigid statutory rules to prevent injustice.
- Equity is not a rigid concept, and its principles are not applied in a vacuum; rather, equity is determined on a case by case basis when justice and fairness so require.

# POTENTIAL HOOK: VIOLATION OF PUBLIC POLICY

- A provision is said to violate public policy if it is injurious or detrimental to the public welfare or public good.
  - See Nat'l Bank of Com. v. Greenberg, 195 Tenn. 217, 226, 258 S.W.2d 765, 769 (1953), EGW v. First Fed. Sav. Bank of Sheridan, 2018 WY 25, 413 P.3d 106, 110 (Wyo. 2018).
- Essentially extreme circumstances.
- Examples of Public Policy Violations:
  - Preventing trustee from making distribution to charitable beneficiary and requiring accumulation of trust assets for 99 years. *Penick v. Bank of Wadesboro*, 218 N.C. 686, 12 S.E.2d 253, 257 (1940).

# POTENTIAL HOOK: VIOLATION OF PUBLIC POLICY

- Examples of Public Policy Violations (cont'd):
  - Absolving trustee of any right to account. *In re Wallich's Est.*, 420 P.2d 40, 43 (Ut. 1966); *Briggs v. Crowley*, 224 N.E.2d 417, 421 (Mass. 1967); *In re JP Morgan Chase Bank, N.A.*, 956 N.Y.S.2d 856 (Sur. Ct. 2012);
    - Alan's corollary: A trustee without any duty to account to anyone is not a trustee.
  - Preventing successor trustee from obtaining communications of prior trustee. *Morgan v. Superior Ct.*, 233 Cal. Rptr. 3d 647,655 (Cal.App. 2018).
  - Absolving a trustee of any duty to exercise reasonable care and prudence regarding the holding of assets without any liability for any decrease in trust value. *Matter of Will of Allister*, 545 N.Y.S.2d 483, 486 (Sur. 1989).

## POTENTIAL HOOK: IMPOSITION OF DUTY WITH POWER

- Trust protector or trust adviser who is afforded powers, may also have associated implied duties to exercise such powers.
  - *McLean Irrevocable Trust v. Patrick Davis, P.C. et al.*, 283 S.W.3d 786 (Mo.App. 2009) (finding trust provisions that afforded trust protector power to remove and replace trustee required trustee to exercise such power if trustee was acting against the purpose of the trust).

## POTENTIAL HOOK: RETAINED DUTIES

- Related or corresponding fiduciary duties not exonerated:
  - Example:
    - A directed trustee is directed by a trust director to invest funds into certain securities.
      - The directed trustee does not have a duty to assess the appropriateness of the investment; but
      - The directed trustee may have a fiduciary duty to make sure the funds are invested in a reasonable time at a reasonable cost.

# POTENTIAL HOOK: OTHER DUTIES NOT EXONERATED

- Duty to inform and advise:
  - A trust director could be required to provide information to a trustee or another trust director to the extent the information is reasonably related to both the powers or duties of the director and the powers or duties of the trustee or other director.
  - A trustee could be required to provide information to a trust director to the extent the information is reasonably related to both the powers or duties of the trustee and the powers or duties of the director.
  - A directed trustee could be required to communicate status of trust to beneficiaries
    - *Rollins v. Branch Banking & Trust Co. of Virginia*, 56 Va.Cir. 147 (2001) (directed trustee liable to beneficiaries for failure to communicate information received regarding investment decisions to beneficiaries and for failure to advise beneficiaries of risks associated with over-concentration).

# POTENTIAL HOOK: OTHER DUTIES NOT EXONERATED

- Duty to Monitor and Advise:

- Where a trust director is given the power to direct investments, the trustee does not owe a duty to advise the grantor or beneficiary of the risks of those investments.
- However, the trustee could still owe a duty to provide periodic reports of trust investments or accountings to the beneficiary and answer questions posed by beneficiaries.
- *In re Rivas*, 2011 WL 32792 (N.Y.Surr. 2011) (in petition for instructions regarding investment committee proposal to invest funds contrary to purposes of trust and intent of settlor, court found that even though trustee was directed trustee as to investments, trustee would still have had accountability if such investments would have completely voided the purpose of the trust.)



# POTENTIAL HOOK: GROSS NEGLIGENCE

- A court could find gross negligence based on totality of conduct (i.e. complete indifference) relating to the trust, not just the directed duty:
- *Hart v. Kline*, 116 P.2d 672 (Nev. 1941):
  - “Gross negligence cannot be precisely defined.”
  - “Gross negligence is equivalent to the failure to exercise even a slight degree of care.”
  - “It amounts to indifference to present legal duty, and to utter forgetfulness of legal obligations so far as other persons may be affected.”
- *Davies v. Butler*, 602 P.2D 605 (Nev. 1979):
  - Gross negligence is manifestly smaller amount of watchfulness and circumstances required of a prudent man. But it falls short of being such reckless disregard of probable consequences as is equivalent to a willful and intentional conduct.”

# POTENTIAL HOOK: WILLFUL MISCONDUCT

- A court may be more inclined to broadly construe willful misconduct depending on the circumstances:
- *Davies v. Butler*, 602 P.2D 605 (Nev. 1979):
  - “[Willful] misconduct involves an intention to perform an act that the actor knows, or should know, will very probably cause harm.”
- Example: *Mennen v. Wilmington Trust Co. et al.*, 2015 WL 1914599 (Del.Ch. 2015):
  - Where trust instrument exonerated trustee for actions taken “in good faith,” found trustee engaged in willful misconduct and bad faith where investing trust assets in investments designed to benefit trustee (as a separate investor in the investments.

## STAYING OFF THE HOOK: CONSIDERATIONS

- Even in age of increasing limitations on liability, it would be prudent to analyze certain considerations:
  - Drafting;
  - Administration;
  - Interactions with beneficiaries; and
  - Court intervention

# STAYING OFF THE HOOK: DRAFTING CONSIDERATIONS

- Nevada trusts are construed according to the Settlor's intent: including a statement of intent regarding exoneration, trust advisers and directed fiduciaries will aid the court in interpreting and construing such provisions.
- Make sure the exoneration provisions do not exceed what is permissible by Nevada law.
- Require that trust adviser directions are clear, in writing, and to be served upon the directed fiduciary.

# STAYING OFF THE HOOK: DRAFTING CONSIDERATIONS

- Clearly detail the duties and responsibilities (including any fiduciary duties or waiver thereof) as to each director and directed fiduciary:
  - For example, if providing a director authority to investigate a particular issue, be sure to delineate whether such authority imposes a duty to investigate.
  - Likewise, as to a directed fiduciary, ensure that the trustee has no other discretionary powers that would be inconsistent with the directions of the trust adviser and has no discretion to refuse such directions.

# STAYING OFF THE HOOK: DRAFTING CONSIDERATIONS

- Make sure trust adviser and directed fiduciary provisions are consistent throughout the trust and not inconsistent with each other or other duties—especially if varying from default Nevada law positions.
  - For example, does a directed trustee have duty to enforce repayment of loans where it has been directed to make the loan?
  - For example, exoneration of liability provisions for a directed trustee may be inconsistent with other duties the trustee may have if it receives information.
  - For example, what are the responsibilities of investment adviser and directed trustee if litigation arises in connection with an investment?

# STAYING OFF THE HOOK: DRAFTING CONSIDERATIONS

- If expansive exoneration provisions are provided to a drafter who also will serve as a trust adviser, the drafter should have full and frank discussion with the settlor regarding those provisions to avoid potential ethical violations for conflict of interest or a finding that such provision given the circumstances violates public policy.
- Best practice would be to have a separate acknowledgement regarding those provisions or an independent attorney review of those provisions.

# STAYING OFF THE HOOK: ADMINISTRATION CONSIDERATIONS

- Recognize potential duties that may be imposed upon the trustee or directors, including:
  - **Duty of Impartiality:** *Matter of W.N. Connell and Majorie T. Connell Living Trust*, 133 Nev. 137, 141, 393 P.3d 1090, 1094 (2017);
  - **Duty to Avoid Conflicts of interest:** *Matter of W.N. Connell and Majorie T. Connell Living Trust*, 133 Nev. 137, 141, 393 P.3d 1090, 1094 (2017);
  - **Duty of Disclosure:** *Klabacka v. Nelson*, 133 Nev. 164, 179, 394 P.3d 940, 952 (2017);
  - **Duty to Avoid Self Dealing:** *Riley v. Rockwell*, 103 Nev. 698, 701-02, 747 P.2d 903, 905 (1987).



# STAYING OFF THE HOOK: ADMINISTRATION CONSIDERATIONS

- Potential duties that may be imposed upon the trustee or directors (continued):
  - **Duty to account:** *In re Millenovich's Estate*, 5 Nev. 161, 177, 1869 WL 2397, \*10 (1869).
  - **Duty of Loyalty:** *Id.*
  - **Duty to Act in utmost good Faith:** *Id.*
  - **Duty of Prudence:** *Id.*
  - **Duty of Diligence:** *Id.*

## STAYING OFF THE HOOK: ADMINISTRATION CONSIDERATIONS

- Develop organizational charts mapping out the duties and functions of the trust advisers and the directed fiduciaries.
- Carefully examine exoneration provisions of the trust to ascertain the scope of the exoneration.
- Even if not required in the trust instrument, implement an administration requirement that the trust adviser provide directions in writing and served upon the directed fiduciary; have the directed trustee respond in writing regarding the directions.
  - Consider amending or decanting trust to include written requirement.

# STAYING OFF THE HOOK: INTERACTIONS WITH BENEFICIARIES

- If concerned about a particular directive or interaction, seek to obtain beneficiary consent and/or waiver:
  - Notice of proposed action (NRS 164.725): regarding the particular action and the acknowledgment or consent to waive questioned duties/liability.
  - Obtain express beneficiary consents (NRS 163.160): regarding the rights, duties, obligations of the trust advisers and/or trustees beneficiary consents.
    - For such consents to be effective, must give beneficiary “full information,” which other courts have held to require apprising the beneficiary of all relevant facts and legal rights relating to the consent.

# STAYING OFF THE HOOK: COURT INTERVENTION

- If concerned about a particular directive or interaction, seek court instruction:
  - NRS 164.015 & 163.180: Petition for instructions permissible by interested person as to the “administration and distribution of the trust, declaration of rights and determination of other matters involving trustees and beneficiaries....”
  - NRS 30.060: Affords additional authority for fiduciary to request that the court enter an order “determine any question arising in the administration of the ... trust.”
    - NRS 30.100: Further permits a court making such declaration to enter relief to effectuate the declaration made by the court.

# QUESTIONS, CONCERNS OR BLANK STARES

