

## Question 1

Sam, a widower, set up a valid, revocable *inter vivos* trust, naming himself as trustee, and providing that upon his death or incapacity his cousin, Tara, should be successor trustee. He did not name any additional trustee. He directed the trustee to distribute the income from the trust annually, in equal shares, to each of his three children, Ann, Beth, and Carol. He specified that, at the death of the last of the three named children, the trust was to terminate, and the remaining assets were to be distributed to his then living descendants, by representation.

When he established the trust, he also executed a valid will pouring over all his additional assets into the trust.

Two years later, Sam died. He was survived by Ann, Beth, and Carol. Within two months, Dave, age 25, began litigation to prove that he was also a child of Sam's, although Sam had never known of his existence.

For three years after Sam's death, Tara administered the trust as trustee. Because Ann had very serious medical problems and could not work, and because Beth and Carol had sufficient assets of their own, Tara distributed nearly all of the trust income to Ann and little to Beth and Carol.

After the court determined that Dave was in fact Sam's child, Dave claimed a share of the trust. Beth and Carol have filed suit against Tara, claiming breach of fiduciary duties. Tara has submitted her resignation, and Beth and Carol have sought termination of the trust so that all assets may now be distributed outright to the beneficiaries now living.

- 1) What interests, if any, does Dave have in the trust assets? Discuss. Answer according to California law.
- 2) Are Beth and Carol likely to be successful in terminating the trust? Discuss.
- 3) Are Beth and Carol likely to be successful in suing Tara? Discuss.

# Question 1

## Answer A

### 1) Will Substitute

Where an inter vivos trust is created, and where the settlor gives a vested future possessory interest in the trust to a grantee, it will be considered a will substitute. Where the settlor has included a clause whereby all of the settlor's assets at the time of his death pour in to the trust for the benefit of the beneficiaries a pourover will is created. The Will requirements must be established to make this valid.

Here, Sam (S) created a valid inter vivos trust, with himself as Trustee and Tara (T) as the successor Trustee for the benefit of his three children Ann (A), Beth (B), and Carol (C). S also provided that at his death all of his other assets should be poured over into the trust for the benefit of A, B, and C.

Therefore, a valid pourover will was created, with each A, B, and C receiving equal shares of all of the assets.

### Dave's (D) right as an omitted child

In general, a child may be disinherited if the child is left out of a will or other testamentary document created by a parent. However, where a child is unknown to the parent at the time the testamentary document is created, and the parent had no reason to know of the child, that unknown child will not be disinherited, and will be able to recover his intestate share of the parent's estate. A child's intestate share in a modern per stirpes system, which is the majority view taken, will be an equal share split at the first level of inheritance, in this case among the children.

Here Sam (S) set up the trust only 2 years ago. D was 25 years old at the time of S's death. Because S was born before the execution of the trust and pourover will, he would generally be treated as disinherited and unable to recover. Here, however, S

was unaware that D was alive or that D was his child at the time the testamentary documents were created. D would be considered an omitted child and have a right to his intestate share. Because A, B, and C were all alive, D would be entitled to 1/4 of S's estate. Because the trust contained all of the assets of S due to the pourover will, this will be where the assets are taken from. Notwithstanding the clause in the trust that requires the assets to be distributed to living descendants, by representation after A, B, and C die, D will not be required to wait for A, B, and C to die before recovering.

Therefore, D will be entitled as an omitted child to 1/4 of the Trust assets.

## 2) Termination by B and C

The power of termination depends on whether or not a trust is revocable or irrevocable. An irrevocable trust is created where the intent of the settlor is to make it as such. Here S expressly stated that the trust is to last until the death of the last of the three named children. The majority view is to find in favor of irrevocable trust, so it is likely that this language will be sufficient to establish an irrevocable trust.

Therefore, an irrevocable trust has been established, and the rules of termination, discussed below, will regard such.

### Termination of irrevocable trust

Termination of an irrevocable trust can be done, either when the settlor and all of the beneficiaries agree while the settlor is still alive, or if all of the beneficiaries agree and it will not frustrate the purpose of the trust, or a merger where the trustee has become the sole beneficiary. An irrevocable trust is created when the express language of the settlor states as such.

Here, although T has not acted according to the will, and has distributed nearly all of the trust income to A and little to B and C, there must still be a mutual agreement between the beneficiaries to terminate that doesn't frustrate the purpose of the trust. The trust

specifically stated that the trust was to be terminated only at the death of the last of the three named children. Just because B and C are unhappy with the way the trust is being distributed does not give them the right to terminate the trust, either without the consent of A, or in the face of clearly stated terms of the trust made by the settlor.

Therefore, B and C will likely not be successful in terminating the trust, but as discussed below may have damages due from T.

### 3) Type of trust established

To a certain extent a trustee's ability to use discretion varies depending on the type of trust that is established. The greatest deference is given to the trustee in two situations, either a support trust or a discretionary trust. Both of these types of trusts, generally, must expressly state that this is the type of trust being established. The purpose of the trust, which is a necessary requirement of a valid trust should determine what type of trust is created.

Here, the T was instructed to distribute in equal shares annually. There was no express statement of purpose that the trust was being set up for distributions based on the discretion of T, nor based on the need for support of A, B, and C. One of these things would have to be established in order to create a special kind of trust that would give T additional discretionary power.

Therefore, the trust is an express trust, neither discretionary nor support, and T will be bound to the fiduciary duties of a trustee discussed below.

### Fiduciary duties of trustee breached by T.

A trustee has a number of duties to the beneficiaries of the trust. Among those duties are a) a duty of care, b) a duty to distribute benefits in accordance with the trust, c) a duty to treat beneficiaries equally, d) and a duty to follow the settlor's instructions. Only in certain circumstances is the trustee allowed to use discretion in how to distribute the

income of the trust, namely a discretionary trust or a support trust. The trust duties to the beneficiary are triggered by a trustee accepting their position as such. Where a trustee has breached their fiduciary duties, they may be held personally liable, and/or may be removed from their position by the court. There are additional remedies not pertinent to this case.

Here, S was the original trustee of the trust and named T as the successor trustee. T either expressly, or at the least by conduct, accepted the position as trustee, and therefore was bound by the duties of a trustee to the beneficiaries of the trust.

Therefore, T owed the duties discussed below to A, B, and C, and any breach of such could result in personal liability and/or expulsion from the trustee position.

a) Duty of care

A trustee has the duty to act as a reasonably prudent person in her dealings as trustee. This includes investing reasonably, making reasonable distribution, and all other activities that a trustee conducts in her role as trustee.

Here, T was distributing nearly all of the trust income to A and very little to B and C. A, however, had a very serious medical problem and could not work, while B and C had sufficient assets of their own. The trust however expressly stated that distribution of the income from the trust annually should be in equal shares to each of A, B, and C.

Notwithstanding the express direction given to T as to distribution it is possible that T may have reasoned that S was not aware nor could he foresee the circumstances of A, B, and C and his real purpose was to ensure that the children were taken care of during their lives.

Therefore, T may have been reasonable in her actions as trustee, but it may be a close call because of the express direction given in the trust. T would likely have to use extrinsic evidence to show that she was acting in accordance with S's real purpose.

b) Duty to distribute in accordance with the trust

A trustee has a duty to distribute in accordance with directions given in the trust instrument. This duty is breached when the trustee acts in a way inconsistent with the specific instruction set forth by the settlor.

Here the trust expressly stated to distribute the trust in equal shares annually to A, B, and C. T, however, decided unilaterally to distribute the majority of the trust income to A and very little to B and C. This was clearly inconsistent with the directions given by S in the trust instrument.

Therefore, T breached her duty to act in accordance with the trust, and will be liable to B and C for the difference between what they were distributed and what they were entitled to under the trust.

c) Duty to treat beneficiaries equal

A trustee should give the same care and deference to each beneficiary of the trust, in accordance with the trust purpose.

Here, T gave sympathy to A because of her medical condition, and was less concerned with B and C because they had "sufficient assets of their own." It is not a fair and equal treatment to penalize a beneficiary because they have assets available to them outside of the trust. To hold that such action by a trustee is allowed, would be to disgorge the settlor of the trust of his ability to leave trust assets to whomever he might choose. A trust is not only set up for individuals who are in need (as discussed above this is not a support trust), but rather for the benefit of whomever the settlor feels he would like to distribute benefit to.

Therefore, T has not treated B and C the same as A and will be liable for a breach of duty, again with the remedies as described above.

d) Duty to follow settlor's instructions

A trustee has a duty to follow the instructions given to him by the settlor.

Here, the instruction was to distribute the shares equally to A, B, and C. T did not, as discussed above, do so.

Therefore, T breached his duty to follow instructions of the settlor.

# Question 1

## Answer B

### 1) Dave's Interest in the Trust Assets

#### Pretermitted Children

Dave was not specifically provided for in the trust instrument set up by Sam. This is because the trust only mentioned Ann, Beth, and Carol. As such, Dave would normally not have any interests in the trust. However, a pretermitted child may be entitled to a stake in the trust if he can show that he is a pretermitted child. A pretermitted child is one who is born or discovered after the execution of a will. In this case, Dave was presumably not born after the execution of the trust and will as he was 25 years old at the time of Sam's death, and Sam executed the trust and will only two years before his death. However, [he] had never known of Dave's existence. Therefore, Dave is a pretermitted child of Sam's, and may be entitled to some of Sam's estate.

A pretermitted child is entitled to what would be his intestacy's share of the deceased's estate. A pretermitted will not be entitled to this share of the estate, however, if the deceased specifically excluded all children from his will, and the intent to do so is shown on the face of the document. That is not the case here, though, as Sam created the trust to distribute income to his three children that he knew about. Additionally, a pretermitted child will not be entitled to any interest in the estate if the deceased provides for the child in another manner, such as an inter vivos trust, that is intended to take the place of the child's intestacy share. Again, this did not happen here because the inter vivos trust did not provide for Dave. Therefore, because Dave is a pretermitted child, and because none of the exceptions apply that would exclude him from having an interest in the deceased's estate, he is entitled to receive what would have been his intestate share of the estate.



Dave's intestate share of the estate would be equal to 25% of the estate. This is because when Sam died, he had four children and was a widower. Also, there is no mention that Sam had any living siblings or parents. All four of Sam's children survived him, and therefore if Sam had died intestate, each child would receive his share based on a per capita calculation. Therefore, each of Sam's four children would be entitled to 25% of his estate if he had died intestate. The calculation of what Dave is entitled to receive will include the value of the trust. This is because the estate is considered to include assets held by the deceased in a revocable inter vivos trust. Here, the trust that Sam created was revocable and inter vivos declaration in trust. Dave will be able to receive his interest in the estate by abating what was given to the other children. This abatement will occur by operation of law, and would mean that Ann, Beth, and Carol would each have their interest reduced from 1/3 of the estate to 25%.

## **2) Termination of the Trust**

There are several manners in which a trust can be terminated. A trust will be terminated when a specific condition in the writing calls for the termination of the trust and is satisfied. In this case, the trust stated that it would terminate at the death of the last of the three named children. Here, all three of the named children are still alive, and therefore the trust will not terminate.

Further, a trust can be terminated when the stated purpose of the trust has been satisfied and all beneficiaries and trustees agree to end the trust. In this case, this option does not appear to be available. Although there was no stated purpose to the trust, it provided for equal payments to each of Sam's children. Therefore, the purpose of the trust appears to be to provide for Sam's children as long as they are living. This purpose is not satisfied as all three children are still living, and can still be provided for. Also, it is not clear that all the beneficiaries would agree to terminate the trust. Only Beth and Carol are suing to terminate the trust, and there is no indication that Ann or Dave would agree to the termination.

In addition, a trust may also be terminated when all beneficiaries agree to terminate the trust. As stated above, it is not clear that all beneficiaries would agree to terminate the trust because there is no indication that Ann or Dave would agree. Also, the trust has further beneficiaries besides the three named children. The trust provides that after the death of the last of the three named children, the remaining assets of the trust were to be distributed to Sam's then living descendants. This is a vested remainder subject to an open class. The class is vested because it is not subject to any conditions precedent, and it is created in an ascertainable group of people (Sam's living descendants). The interest does not violate the rule against perpetuities, which states that for an interest to be valid, it must vest within 21 years of some life in being at the creation of the interest. Here, the interest will vest when the last of the three named children dies. Therefore the interest must and will vest within 21 years of a life in being at the creation of the interest. Because this class has an interest in the trust, they are beneficiaries of the trust. If the trust is to be terminated due to consent of all the beneficiaries of the trust, they must also consent. There is nothing to indicate that they would consent to the termination of the trust, and therefore Beth and Carol will not be successful in terminating the trust.

Beth and Carol may additionally claim that the trust should be terminated because Tara, the sole trustee, resigned from her position, and because the trust itself does not name any additional trustees. However, this argument will be unsuccessful. Courts will not allow a private express trust to fail for lack of trustee. Instead, a court will merely appoint a new trustee. Here, even though the trust itself does not provide for any additional trustees, the court will appoint someone else to serve as trustee rather than letting it fail.

### **3) Fiduciary Duties of a Trustee**

Beth and Carol will likely be successful in suing Tara, as she has breached several of her duties as the trustee. A trust creates a fiduciary type relationship with respect to property that is held by the trustee for the benefit of beneficiaries. The trustee

must satisfy those fiduciary duties, and if she fails to, may be personally liable for all losses or damages that result to the trust.

### **Duty of Loyalty**

A trustee must satisfy the duty of loyalty by acting in good faith and in the best interests of the trust and beneficiaries. A trustee must not act for her own benefit. Further, a trustee must not favor certain beneficiaries over others. Here, Tara did nothing to show that she was acting for her own benefit. However, Tara was favoring Ann over the other beneficiaries. Tara was doing this because Ann had serious medical problems and could not work, and because Beth and Carol had sufficient assets of their own. Despite her good motives for acting such, though, Tara still violated her duty of loyalty. Her actions specifically favored Ann over the other two beneficiaries. Further, her actions violated the explicit instructions that were contained in the trust and required her to distribute the income from the trust annually and in equal shares to each of the children. Therefore, Beth and Clara could successfully show that Tara breached her fiduciary duty with respect to the trust.

### **Duty of Care**

Additionally, a trustee must satisfy a duty of care by acting in good faith as a reasonably prudent person would with respect to the trust. Here, Tara failed to follow the explicit instructions contained in the trust that required she distribute the income in equal shares to each of the children by providing nearly all the income to Ann. This failure to follow explicit instructions shows that Tara was not acting as a reasonably prudent person would act with respect to the trust. Rather, a reasonably prudent person would follow the instructions contained in the trust. Therefore, Beth and Carol could show that Tara had also breached her fiduciary duty of care.

## **Other Duties**

It is possible that Tara violated other fiduciary duties, such as the duty to invest, the duty to provide accountings to the beneficiaries, the duty to label trust funds, and the duty to keep trust funds separate from other funds. However, the facts do not indicate that Tara breached any other fiduciary duties she had with respect to the trust.

## **Remedies**

Having violated her fiduciary duties, Tara may be personally liable to the beneficiaries. Beth and Carol could sue Tara for damages of the amount of income that they should have been receiving under the trust. In the alternative, Beth and Carol could sue to have a constructive trust created from the excess income that Ann received over what she was entitled to receive from the trust. In such a scenario, Ann would hold the excess income as a constructive trustee, and would be required to return it to Beth and Carol.