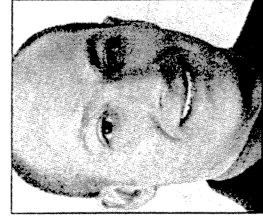


Troubled times for trustees

BY MICHAEL H. FRIEDMAN



Lawsuits against trustees typically increase during turbulent economic times, and today's volatile financial climate is no exception. The number of such lawsuits has surged this year as beneficiaries try to recoup investment and income losses by taking fiduciaries, especially trustees, to court.

Even after the economy recovers, the threat of litigation for past actions remains. However, banks, attorneys, accountants and other trustees can reduce the risk that they will be sued, or, if they are sued, win the case if they are diligent in their conduct and increase their communication with beneficiaries.

There are numerous factors encouraging beneficiaries to file suit against trustees, including if:

- Beneficiaries have lost wealth because their trust accounts have suffered losses;
- Beneficiaries are not realizing as much income as they have in the past because of today's historically low interest rates;
- Beneficiaries are savvy about finance and are demanding more from their fiduciaries and trustees.

A fiduciary is a person or an institution that is given the authority to act on behalf of someone else. The Latin root of the word, *fidere*, means "to trust." In general, fiduciaries are not held liable for investment losses unless the losses are proven to be the result of fiduciary negligence. Therefore, the courts will look to the trustee's conduct, not necessarily the financial performance of the trust's investments, in making a decision. However, the conduct of a corporate fiduciary, such as a bank or investment manager that holds itself out as having special investment skills, will be held to a higher standard than an individual fiduciary without such special investment skills.

Accordingly, corporate trustees should be as diligent as possible. They should review the specific securities and assets in a portfolio to analyze risk and ensure diversification, as well as stay on top of market trends. The trustee should schedule periodic portfolio reviews with the beneficiaries and account to the beneficiaries at least every five years.

Communication is just as important. To improve communication with beneficiaries, trustees should provide monthly statements – even if not stipulated – in addition to the required annual statement. They should ascertain the needs of the beneficiaries and discuss what they expect the trust to provide for them. And, no matter how busy

they are, trustees should respond quickly to beneficiary telephone calls and written communications. In other words, trustees should operate with as much transparency as possible.

To make sure they are doing everything to protect themselves from lawsuits, fiduciaries would be wise to review their conduct and policies with a litigation attorney specializing in trusts and estates, who regularly deals with these issues in the courtroom. Here are several recommendations a trusts and estates litigator might suggest:

- If the trustee is a bank or trust company, it should abide by its established policy, and communicate that policy to all beneficiaries. If the trustee is an individual, he or she should establish a policy, communicate that policy to beneficiaries, and adhere to it;
- Many beneficiaries want a predictable income stream, yet a trustee is obligated in most instances to maintain a diversified investment portfolio designed to provide both income and growth. Trustees should therefore consider implementing a unitrust, in which a certain percentage of the fair market value of the trust property is paid to the beneficiary each year, regardless of the actual income earned. The unitrust approach allows a trustee to diversify and invest for the overall well-being of the trust without having to focus on achieving a specific income stream;
- Be responsive and communicate with beneficiaries on a regular basis. Provide beneficiaries with monthly and annual statements. Hold regularly scheduled meetings (at least once a year) to solicit beneficiary input, and respond quickly to telephone calls, emails, and letters.

I also recommend that corporate fiduciaries choose their clients carefully. They should routinely research beneficiaries to see if they have a history of litigation. Find out if there are extraordinary conflicts between either specific beneficiaries or specific classes of beneficiaries, such as a second wife versus children from the first marriage.

By keeping careful records of its conduct and communications with beneficiaries, a corporate trustee can demonstrate it has upheld its fiduciary duty. Such diligence will make it hard for a disgruntled beneficiary to prove otherwise.

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