CAPACITY, STANDING AND JURISDICTION

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CHAPTER 23

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BAR ADMISSIONS

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PROFESSIONAL ACTIVITIES

- State Bar of Texas, Real Estate, Probate and Trust Law Sections, Trust Code Committee
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CLE PRESENTATIONS AND PAPERS

- *Informal Demand or Formal Discovery: The Debate on Obtaining Information from Fiduciaries Under Their Duty to Disclose*, State Bar of Texas, Fiduciary Litigation Beyond the Basics, 2011 (On panel discussion with the Hon. Guy S. Herman, Travis County Probate Court No. 1; Mary E. Haught and Jeff T. Knebel, paper by Laurie Ratliff)
- *Exculpatory Clauses,* Co-Author Frank N. Ikard, Jr., Co-Speaker Jerry Frank Jones, Texas State Bar, Trial of a Fiduciary Litigation Case, December 2009

COMMUNITY ACTIVITIES

- Founding member of The Fifty, an affiliate of The Seton Fund, which is a group of next generation leaders dedicated to supporting the future of University Medical Center Brackenridge and academic medicine in Central Texas – 2011 to Present
- Austin Habitat for Young Professionals - 2009 - Present
- Rhodes College Austin Alumni Chapter, Co-VP – 2009 - Present

EMPLOYMENT HISTORY

- Ikard Golden Jones, P.C., September 2009 - Present
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I. INTRODUCTION

When beginning a case, it is vital to ensure that all parties are named in the correct capacity, that the plaintiffs have standing to bring suit, and that the court has personal jurisdiction over all parties. This paper addresses the issue of capacity as it relates to trustees being sued in their individual and representative capacity. It also covers the issue of standing to bring a trust action, particularly regarding the rights of remote contingent remaindermen, as well as beneficiaries of trusts where the trustee, settlor or a beneficiary hold an interest that is equivalent to a fee simple interest in the trust. Finally, the paper discusses personal jurisdiction over "necessary parties" in a trust lawsuit, when those necessary parties are non-residents.

II. CAPACITY

Though it may seem like a minor issue, capacity in trust cases is very important, and if ignored, can have serious consequences on the outcome of your case. The issue of capacity in trust lawsuits generally involves whether a lawsuit is brought by or against a trustee in a representative capacity, individual capacity, or both. This decision has particular importance regarding damages. It will determine the source of funds from which you may collect if suing the trustee, and it will determine to whom damages will be paid.

But the most important and often overlooked concept to remember: A trust is not a legal entity. Never sue a trust, sue the trustee.

A. Fred, Trustee and Fred the Individual are Two Different People.

A person who is sued in his representative capacity is legally regarded as a person distinct from the same person in his individual capacity and is a stranger to his rights or liabilities as an individual.[1] Likewise, a person who sues in his representative capacity is legally regarded as a person distinct from the same person in his individual capacity.[2] Acts performed by the same person in two different capacities are generally treated as the transactions of two different legal personages.[3]

B. Effect of Rule

a. If you are suing a trustee who has breached his fiduciary duties and you are seeking money damages, you should sue him in both his trustee *and* individual capacities to maximize recovery potential. There are certain breaches of fiduciary duty that open a trustee to personal liability. For instance, if a trustee misappropriates trust funds, you want to be able to access his personal funds to recover damages. Likewise, if a trustee does not make trust funds productive within a reasonable period of time, the trustee may be personally chargeable with interest. *Langford v. Shamburger*, 417 S.W.2d 438 (Tex. Civ. App.—Fort Worth 1967, writ ref'd n.r.e.), *disapproved of on other grounds by Tex. Commerce Bank, N.A. v. Grizzle,* 96 S.W.3d 240, 249–50 (Tex.2002). If you don't sue the trustee individually, you cannot recover damages from his personal assets because a court may only award damages against a person over whom it exercises jurisdiction.

b. If your client is a beneficiary suing the trustee, the trustee will likely use trust assets to pay his attorney's fees to defend himself in litigation, which means your client is essentially paying your fees *and* the trustee's fees. However, under Tex. Property Code § 114.064, in a proceeding brought under the Code, the court may award costs and reasonable and necessary attorney's fees as may seem equitable and just. Thus, if you have sued the trustee in his individual capacity, you should request that the Court require the trustee pay both his and your attorney's fees out of his personal assets.

c. Most courts are reluctant to award damages out of a trustee's personal assets, absent a certain level of malfeasance. However, many courts will award a plaintiff beneficiary's attorneys' fees to be paid from the trust's estate. The trustee should be sued in his capacity as trustee so that such funds are accessible.

d. It is our firm's standard practice to sue the trustee in both his individual and trustee capacity, and we

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[1] *Elizondo v. Texas Natural Resource Conservation Commission*, 974 S.W.2d 928, 931 (Tex. App.—Austin 1998, no writ), citing *Alexander v. Todman*, 361 F.2d 744, 746 (3d Cir. 1966); *Bender v. Williamsport Area Sch. Dist.*, 475 U.S. 534, 543-44 & n. 6, 106 S.Ct. 1326, 89 L.Ed.2d 501 (1986); *Airlines Reporting Corp*. v. S & N Travel, Inc., 58 F.3d 857, 862 (2d Cir. 1995) ("Where a party sues or is sued in a representative capacity, however, its legal status is regarded as distinct from its position when it operates in an individual capacity"); *McGinnis v. McGinnis*, 267 S.W.2d 432, 435 (Tex. Civ. App.—San Antonio 1954, no writ) ("William L. McGinnis, the individual, is not the same party as William L. McGinnis, the next friend of Janie Barr's estate and person.").

[2] *Elizondo v. Texas Natural Resource Conservation Commission*, 974 S.W.2d 928, at 931 (Tex. App. – Austin 1998, no writ); *In re Guetersloh*, 326 S.W.3d 737, 739-40 (Tex. App. – Amarillo, 2010, no pet.) (individual could appear pro se in court proceeding but not in his capacity as trustee).

[3] *Bender v. Williamsport Area Sch. Dist.*, 475 U.S. 534, 543-44 & n. 6, 106 S. Ct. 1326 (1986).

typically address attorney's fees in our original petitions as follows:

> Plaintiffs PRAY that this Court award them attorneys' fees and costs, including their attorneys' fees and costs incurred on appeal, pursuant to Texas Trust Code § 114.064, against [Trustee name], individually.
>
> In the alternative, Plaintiffs PRAY that this Court award them attorneys' fees and costs**,** including their attorneys' fees and costs incurred on appeal, pursuant to Texas Trust Code § 114.064, to be paid by the Trustee of the Trust from the assets of the Trust.
>
> Additionally, Plaintiffs PRAY that, pursuant to Texas Trust Code §114.064, this Court disallow the payment of any of Defendant's attorneys' fees, costs and/or litigation expenses from the trust estate of the Trust and, to the extent that any such fees, costs or expenses have been previously paid out of the trust estate of the Trust, Plaintiffs PRAY that this Court order that such sums be reimbursed by Defendant, individually, to the trust estate of the Trust.

If your client is a trustee suing a third party in his representative capacity, then any damages recovered from the third party will go back into the trust estate, not your client's pocket. Make this clear to your client because there are situations where the client who does not understand this may be sorely disappointed.

For example, your client, Mary, is a co-trustee who is suing her co-trustee, Bob, for misappropriation of $1 million. Mary is also a beneficiary, and all of the other beneficiaries could care less about the lawsuit. Mary carries the water for everyone for 5 years, and at the end of it all, Mary gets a $1 million recovery from her co-trustee. That $1 million does not go into Mary's pocket. It goes into the trust estate. Depending on the terms of the trust, Mary may never even see a dime of that money. However, as co-trustee, Mary has a fiduciary duty to compel Bob to redress his serious breach of trust, or she, as co-trustee, is also liable. Tex. Property Code § 114.006. If you do not explain this to Mary up front, you will have a lot of explaining to do at the end when she expects to take home $1 million and does not.

The same is true if your client is a beneficiary that is suing in a derivative capacity on behalf of a trustee. The recovery of damages goes to the trust, not the beneficiary.

Always correctly identify each party's capacity in all court documents. If you sue a trustee in both his individual and trustee capacities, be sure to serve him in both capacities. If your client is sued in both capacities, be sure to answer in both capacities. If you do not answer in both capacities, then the opposing party can get a default judgment against your client in the capacity that he did not answer. If you are filing a special appearance, be sure to file it in both capacities. I recently saw a case where the defendant filed a special appearance solely in his individual capacity. The defendant likely waived his special appearance in his capacity as trustee.

Likewise, make sure to appeal in all capacities. In *Elizondo*, the plaintiff sued in her individual capacity and her capacity as representative for some heirs. *Elizondo,* 974 S.W.2d at 931. However, Ms. Elizondo's notice of appeal was couched in singular terms: "NOW COMES PLAINTIFF, Mildred Elizondo, a person, and gives notice of her intent to appeal the judgment in this case." The court held that Ms. Elizondo only perfected the appeal in her individual capacity and not in her representative capacity.

III. STANDING

This section addresses two types of standing in trust matters: 1) standing to bring a trust action; and 2) standing to compel an accounting under Tex. Prop. Code § 113.151. Standing is not as straightforward as it seems, and it is a changing area of the law.

A. Standing to Bring a Trust Action.

The ability to bring an action related to a trust is limited – the Texas Trust Code explicitly limits standing in such actions to "interested persons" – in other words, persons with some threshold interest in the trust. TEX. PROP. CODE § 115.011(a) ("any interested person may bring an action under § 115.001 of this Act").

An "interested person" is defined in the Property Code as:

> A trustee, beneficiary, or any other person having an interest in or claim against the trust or any person who is affected by the administration of the trust. **Whether a person, excluding a trustee or named beneficiary, is an interested person may vary from time to time and must be determined according to the particular purposes and matter involved in the proceeding**.

Tex. Prop. Code § 111.004(7) (emphasis added).

A "beneficiary" is defined as "a person for whose benefit property is held in trust, regardless of the nature of the interest." Tex. Prop. Code § 111.004(2).

An "interest" is "any interest, whether legal or equitable or both, present or future, vested or contingent, defeasible or indefeasible." Tex. Prop. Code § 111.004(6).

1. How far does the definition of "interested person" extend?

If the first sentence of Property Code § 111.004(7) is read in isolation, then it appears that a determination of "interested person" status (and thus standing) is clear-cut. The first sentence appears to say that *any* person who is a beneficiary of a trust or who has any other "interest" in the trust is automatically an "interested person" in that trust, and therefore under § 115.011(a) would have standing to sue.

However, the standing conferred under the Property Code is not black and white – rather, when the plaintiff is not a trustee or a *named* beneficiary, the trial court must determine in its discretion whether the plaintiff is an "interested person" for the "particular purposes and matter involved in the proceeding." Tex. Prop. Code § 111.004(7).

While a person might have an "interest" in the trust,[4] he still may not be an "interested person" for standing purposes if the court determines his interest is too speculative and remote to bring the particular action. See *id.*

2. Contingent vs. vested remaindermen.

A contingent remainder interest arises either when taking possession is subject to a condition precedent (such as when taking is contingent upon surviving the previous interest holder), or when a remainder is created in favor of unascertained persons. Black's Law Dictionary 1294 (7th ed. 1999).

A person's heirs cannot be ascertained until he dies. *Glenn v. Holt*, 229 S.W. 684, 685-86 (Tex. Civ. App.—El Paso 1921, no writ). Therefore, any remainder to the "heirs" of a person is a remainder created in unascertained persons, and is thus a contingent remainder. *Id.* at 686. Further, to become an heir, it is a condition precedent to survive the person from whom the heir would take. Restatement of Property § 249 cmt. e (1940).

A remainder vests, on the other hand, when it is in an ascertainable person and no conditions precedent exist other than the termination of prior estates. *In re Townley Bypass Unified Credit Trust*, 252 S.W.3d 715, 717 (Tex. App.—Texarkana 2008, pet. denied). For example, if the trust says that on A's death, the trust terminates and goes to B, B has a vested remainder interest.

3. Are speculative or remote contingent remaindermen "interested persons?"

Equity requires that someone have standing at all times to assert causes of action against a trustee on behalf of the remainder beneficiaries. An issue arises, however, where a person sues a trustee, and that person has a very remote or speculative chance of taking under a trust. Technically such person may fall under the definition of "beneficiary" because he has a contingent remainder interest, however, should that person be permitted to engage in costly litigation if it is almost impossible that he will take any part of the trust? There is a developing trend in trust law to limit standing in situations where the contingent remainderman's interest is remote.

The strength of a beneficiary's interest in a trust can be measured on a continuum, with one end of the continuum reflecting a beneficiary who has a strong interest in the trust, for instance, a current beneficiary, and the other end of the continuum reflecting a beneficiary who has a highly speculative and remote remainder interest in the trust. While in the typical trust, the number of potential beneficiaries who will actually become beneficiaries is only a handful of people, when the term "heirs" is used, the pool of potential beneficiaries expands exponentially because heirs are not determined until a person's death. That pool may include distant cousins, great grandchildren, nieces, nephews, aunts, uncles, and essentially any person who in some fathomable way could be considered a prospective heir at law.

In the *Davis* case, a trust was created by the plaintiff's mother for the benefit of the plaintiff's children. *Davis v. Davis*, 734 S.W.2d 707, 709-10 (Tex. App.—Houston [1st Dist.] 1987, writ ref'd n.r.e.). The plaintiff argued he had standing to sue the trustees of the trust because, if one of his children died intestate, he would inherit that child's interest in the trust. *Id.* at 709. The court held that the plaintiff did not have standing based on his claim that he is a *potential* beneficiary of the trust because "the possibility of inheritance does not create a present interest or right of title in property." *Id.* at 709. The right to inherit does not vest until the death of the intestate. *Id.* at 709. Thus, the plaintiff could not sue for the enforcement or adjudication of a right in property that he *expected* to inherit because he had no present right or interest in the property. *Id*. at 709-710.

Consider a trust where A is the current beneficiary, and the remaindermen are A's "heirs." A's living relatives include 5 children, 10 grandchildren, two brothers, two parents and a great-great-niece. All of these people are A's prospective heirs, and as such, all have a contingent remainder in the trust, including the great-great niece. Under a "common disaster" scenario, that great-great niece may find herself *fortunate* enough to become a current

[4] An "interest" means "any interest, whether legal or equitable or both, present or future, vested or contingent, defeasible or indefeasible." TRUST CODE § 111.004(6) (West Supp. 2009).

beneficiary of the trust upon the simultaneous death of A and her more closely related kin. However, such likelihood is very low and speculative. The great-great-niece, therefore, has a valid, but very remote and speculative contingent remainder interest.

According to some authorities, the mere fact that the great-great niece has *some* remainder interest grants her standing as an "interested person" and she could therefore sue the trustee of A's trust in spite of the fact that the chance of her taking under the trust is almost entirely implausible. The effect would be that a person with little chance of ever becoming a beneficiary of the trust could significantly impact the trust and potentially alter its course forever, to the detriment of the beneficiaries who will in reality be the takers.

You may wonder why a great-great niece would waste her money suing in such a situation. After all, it will cost her significant attorney's fees, and she is unlikely to take under the trusts. But consider a trust worth $100 million. It may be worth it to the trustee to pay the great-great niece some money to drop the lawsuit rather than spend millions in litigation. In effect, the great-great niece, who would otherwise get nothing, has secured for herself a nice payout.

The Trust Code standing statute allows the court flexibility to recognize that, although technically when named in the trust, a potential heir has a remainder interest in a trust, he is no different in substance than a potential intestate heir with a mere expectancy who, it has been held, is not an "interested person" in a trust (because his interest is too speculative). *See Davis,* 734 S.W.2d 707.

4. General rules on standing and remote contingent beneficiaries.

Courts and experts on trust law are increasingly recognizing that a contingent beneficiary does not have standing to sue where there is a beneficial interest in the trust that is equivalent to fee simple ownership, for instance, where the contingent beneficiary's interest is subject to a right of revocation, an unrestricted right of withdrawal by the primary beneficiary, or a general power of appointment.[5]

a. Revocable Trusts.

(1) When a settlor may revoke the trust.

Suppose Settlor creates a revocable trust for the benefit of C & D, remainder to E at termination. Settlor appoints T as trustee. Until Settlor either dies or becomes legally incapacitated, Settlor may revoke the trust at any time, in the same way that a testator may revoke or rewrite a will. Beneficiaries C, D and E are at the mercy of Settlor, and they better stay in the good graces of Settlor if they want to continue to be beneficiaries of the Trust.

In a revocable trust situation, a settlor's power of revocation gives him so much control over the trust that it is equivalent to outright ownership of the trust assets. Thus, the trustee's duties are owed exclusively to the settlor during the settlor's lifetime.[6] The trustee of a revocable trust cannot be held liable for conduct that otherwise is actionable if the competent settlor knowingly approves such action.[7] While the settlor has mental capacity and is alive, the trustee of the revocable trust, while clearly subject to usual fiduciary duties to the settlor, is not accountable to and is under no duty to provide information about the trust to non-settlor beneficiaries.[8]

In *Moon v. Lesikar* 230 S.W.3d 800 (Tex. App. -- Houston [14th Dist.] 2007, pet. denied) the trust was settled by Lesikar, and his daughter Carolyn, sued over transactions Lesikar made with the trust.[9] The court determined Carolyn was not an "interested person" as long as Lesikar was alive because he could revoke the trust at any time, which would remove Carolyn as a beneficiary. Since Carolyn was not an "interested person," the court found she did not have standing to sue regarding the trust.[10]

An interesting question arises when the settlor of a revocable trust dies or becomes mentally incapacitated and the trust thereby becomes irrevocable. At that time, does the beneficiary have standing to sue the trustee for prior breaches, and if those breaches occurred years ago, is the beneficiary barred by limitations from suing? There is a reasonable argument that the beneficiary does have standing to sue for prior breaches, and that the statute of limitations begins running on the settlor's date of death or incapacity.

According to Bogert, after the death of a settlor of a revocable trust, a trustee is accountable to the remainder beneficiaries for its administration of the trust during the settlor's lifetime, when the trustee breached its duty during the settlor's lifetime and the settlor did not consent or know about such breach. Bogert, *Trusts & Trustees* (Third Ed.) § 964. The remainder beneficiary may sue when the breach subsequently affects the interest of the vested beneficiary. *Brundage v. Bank of America*, 996 So.2d 877, 882 (Fla. Dist. Ct. App. 4th 2008).

[5] *See Scott and Ascher on Trusts* § 17.4 and 17.5 (5th ed. 2007).

[6] *Id.; Brundage v. Bank of America*, 996 So.2d 877, 882 (Fla. Dist. Ct. App. 4th 2008).

[7] *Id.*

[8] *Id.*

[9] *Moon v. Lesikar 2*30 S.W.3d 800, 804 (Tex. App. -- Houston [14th Dist.] 2007, pet. denied).

[10] *Id.* at 804.

For instance, where a trustee different from a settlor removes property or money from a revocable trust, those withdrawals could be made without the settlor's knowledge or consent. *Siegel v. Novak*, 920 So.2d 89, 95 (Fla. App. 2006); cited as persuasive by Moon v. Lesikar, 230 S.W.3d 800, 804 (Tex. App.—Houston [14th Dist] 2007, pet. denied. In such situation, after the death of the settlor, the beneficiaries have standing to challenge pre-death withdrawals from the trust that are outside the purposes authorized by the trust and which are not approved or ratified by the settlor. *Id*.

As stated by the court in *Siegel v. Novak*, "a trustee should not be able to violate its fiduciary duty and authorize withdrawals contrary to the provisions of the trust, and yet escape responsibility because the settlor did not discover the transgressions during her lifetime." *Siegel*, 920 So.2d at 96. Where a beneficiary has an interest in the corpus of the trust after the death of the primary beneficiary, the remainder beneficiary has standing to challenge the disbursements because they have alleged a concrete and immediate injury caused by the trustees, which could be redressed. *Id*. Absent this remedy, a trustee's wrongdoing that is concealed from the settlor during her lifetime would be rewarded. *Id*. A trustee "should not be permitted to escape the duty to account for property which …[a] decedent put into [one's] possession and over which [one] exercised control both before and after the decedent's death." *Id.* (internal citation omitted).

In this situation, would the beneficiary be barred from suing the trustee if the beneficiary knew about the breaches that occurred 15 years ago but could not sue because the trust was revocable, and, thus, the beneficiary did not have standing?

In applying a statute of limitations, "a cause of action generally accrues at the time when facts come into existence which authorize a claimant to seek a judicial remedy." *Murray v. San Jacinto Agency, Inc.*, 800 S.W.2d 826, 828 (Tex. 1990). As the Tyler Court of Appeals stated, "It is axiomatic that standing is the first prerequisite to maintaining a suit." *Polaris Indus. V. McDonald*, 119 S.W.3d 331, 338 (Tex. App.—Tyler 2003, no pet.) citing *Hunt v. Bass*, 664 S.W.2d 323, 324 (Tex. 1984). It is arguable that without standing, the cause of action has not accrued because the facts are not in existence authorizing a judicial remedy. Thus, for a beneficiary of a revocable trust, limitations do not begin to run until the day the settlor dies or becomes incapacitated because only then have facts come into existence that authorize the beneficiary to seek a judicial remedy (i.e. he now has standing to enforce the trust).

(2) When a trustee may revoke the trust.

If the trustee holds the power to revoke or amend the trust, then, according to *Restatement (Third) of Trusts* (2012), no beneficiary should have standing to maintain a cause of action against him. This is because the trustee has what is equivalent to fee simple absolute.

Example: A is trustee of a trust for the benefit of B, C and D. A is not incapacitated and holds a presently exercisable and unrestricted power to modify or revoke the trust. The trust provides that upon A's death, the remainder of the trust estate passes to E. Neither B, C, D or E should have standing to sue A, the trustee. This is because A's power to modify the trust is equivalent to fee simple ownership.

(3) When a beneficiary may revoke the trust.

If a beneficiary who is not the trustee, has the unrestricted power to revoke or amend the trust, then the issue becomes much more complicated.

Example: A is the trustee of a trust for the benefit of B, C and D. B is not incapacitated and holds a presently exercisable and unrestricted power to modify or revoke the trust. The trust provides that, upon termination, the entire trust estate passes to E. In this case B, C, D and E should all have standing to sue A, the trustee. B, of course, may eliminate C, D or E's equitable interest in the trust (and consequently, their standing to sue) by modifying the trust. Thus, it might not be in their best interest to sue and risk angering B and being cut out of the trust completely.

Here, the beneficiaries are in a difficult position if they know A is stealing. If B is opposed to holding A accountable, then the beneficiaries may have to choose not to sue because otherwise they risk B revoking the trust. If B dies or becomes mentally incapacitated within the statute of limitations period, then the beneficiaries can sue A for his breaches of fiduciary duty. However, if B does not die or become mentally incapacitated within the limitations period, then the beneficiaries have likely waived their claims.

b) Powers of Appointment

(1) Presently Exercisable Special Powers of Appointment:

The holder of a special or limited power of appointment cannot exercise the power in favor of himself, his estate, his creditors or the creditors of his estate.

i. Trustee

If a trustee holds a presently exercisable special power of appointment, then standing of the taker in default of exercise of the power is not affected unless the power has been actually exercised.

Potential appointees of the power of appointment should not have standing to sue the trustee because they are not beneficiaries of the trust.

If the power of appointment has been actually exercised, then the donees under such power should have standing to sue the trustee. The beneficiaries who would have taken had the power not been exercised lose standing once the power is exercised.

ii. Beneficiary

If a beneficiary (who is not serving as trustee) holds a presently exercisable special power of appointment, then standing should not be affected unless such power is actually exercised. The results are the same as a trustee holding a special power of appointment.

Example 1: A is the trustee of a trust for the benefit of B, C and D. A is not incapacitated and holds a presently exercisable special power of appointment over the remainder of the trust to his lineal descendants who are currently E, F and G. The trust provides that upon the death of the survivor of B, C and D, the entire remainder of the trust estate passes (in the event that A does not exercise his special power) to H. If A has not exercised his special power, then B, C, D and H may sue the trustee. E, F and G may not sue the trustee because they are not beneficiaries of the trust.

Example 2: Same example as 1 above, but A exercises his special power in favor of F. B, C, D and F should have standing to sue the trustee. E and G should not have standing to sue the trustee because they are not beneficiaries of the trust. H should no longer have standing to sue the trustee because his equitable interest in the trust has been terminated by A's exercise of his special power.

Example 3: Same example as 1 and 2 above except that B, who is not serving as trustee, possesses the presently exercisable special power of appointment. The results are the same as Examples 1 and 2.

2) Presently Exercisable General Power of Appointment:

The holder of a general power of appointment may appoint the trust property in favor of anyone he chooses, including himself or his own estate.

i. Trustee

If the trustee has the legal capacity to exercise a presently exercisable general power to appointment over the trust estate of the trust, then no beneficiary should have standing to maintain a cause of action against him.

ii. Beneficiary

If the beneficiary has the legal capacity to exercise a presently exercisable general power of appointment over the trust estate of the trust or to appropriate or consume the entire trust estate of the trust, then no other beneficiary has standing.

Bogert equates the impact of the primary beneficiary's powers of appointment and of withdrawal on a contingent remainder beneficiary with that of a settlor's power to revoke a revocable trust:

> [T]he holder of a presently exercisable general power of appointment, or a power of withdrawal that is not subject to a standard, has unilateral, unrestricted access to trust assets subject to the power, and thus has the functional equivalent of outright ownership of those assets. As a result, the holder of such a power is, with respect to the assets subject to the power, in the same position as if the holder were the settlor of a revocable trust of those assets …. (emphasis added).[11]

Like a revocable trust, where a trust grants a primary beneficiary a power of withdrawal or a general power of appointment, the primary beneficiary has the equivalent of ownership of the assets in the trust.[12]

Example: A is trustee of a trust for the benefit of B, C and D. A is not incapacitated and holds a presently exercisable general power of appointment over the trust estate. The trust provides that if A does not exercise his power then, upon termination, the entire trust estate passes to E. No one should have standing to sue A.

3) Testamentary Powers of Appointment.

The fact that either a trustee or beneficiary holds a testamentary power of appointment (either general or special) should not affect the standing of any beneficiary of the trust to sue the trustee. This is because the exercise of such a power is not effective until the date of the death of the holder of the power, and although a person that holds the power may execute a will that exercises the power of appointment, the will is not effective until his death. Before death, the testator can revoke the will and name new appointees or choose not to exercise the power of appointment at all. Thus, the potential appointees of the power should not have standing to sue the trustee because they are not beneficiaries of the trust until the person holding the power of appointment dies.

In *Cote v. Bank One, Texas, N.A.*, No. 4:03-CV-296-A, 2003 WL 23194260 (N.D. Tex. Aug. 1, 2003),

[11] *Bogert, Trusts & Trustees* (Third Edition) § 964.
[12] *Id.*

Mrs. Haltom, the primary beneficiary of the trust, held a testamentary power of appointment. Cote, Mrs. Haltom's daughter, sued the trustees of the Haltom Trust while her mother was still alive.[13] During the suit, Mrs. Haltom signed an affidavit stating that she had executed a will exercising her testamentary power of appointment and designating her residuary estate as the beneficiary of the corpus of the trust, and stating that her daughter, Cote, was a primary beneficiary of such residuary estate.[14] In determining whether Cote was an "interested person" under the Trust Code, the court noted that a potential beneficiary of trust assets does not have standing to sue, and that there was no certainty that Cote would inherit because, despite her assertions to the contrary, Mrs. Haltom could elect to amend her will and revoke the power of appointment.[15]

Interestingly, Cote was apparently also named a remainder beneficiary of the trust. Because of the existence of the power of appointment, Cote held a contingent remainder interest. The court held that a contingent remainder beneficiary of a trust does not have standing to sue where the primary beneficiary held a testamentary power of appointment because it was uncertain whether the remainder beneficiary would ever take under the trust.[16] In *Cote*, regardless of Cote's remainder status, the court held that she was not an interested person because of the possibility that her mother would subsequently exercise her power of appointment in a way that would remove Cote as a beneficiary of the Trust. *Id*. at *4.

The holding in *Cote* is partially in line with the authorities, however, the holding that a contingent remainder of a trust has no standing where there is a testamentary power of appointment, is not consistent with the authorities. If this were the case, then there are no remaindermen who can enforce the trust. A trustee would be permitted to violate the trust and, for instance, improperly distribute all funds to the beneficiary that holds the power of appointment, without recourse.

c. Standing to Seek an Accounting

The question of whether a beneficiary has sufficient interest to seek an accounting is separate from whether a beneficiary has sufficient interest to bring a trust action.

Under Tex. Prop. Code §111.0035(b), the terms of an *irrevocable* trust may not limit a trustee's duty to respond to an accounting demand under Section 131.151 "if the demand is from a beneficiary who, at the time of the demand (1) is entitled or permitted to receive distributions from the trust; or (2) would receive a distribution from the trust if the trust terminated at the time of the demand."

Under Tex. Prop. Code § 113.151(a), a "beneficiary" may seek to have a court "require the trustee to deliver a written statement of account to all beneficiaries on finding that the nature of the beneficiary's interest in the trust or the effect of the administration of the trust on the beneficiary's interest is sufficient to require an accounting by the trustee." § 113.151(b) says that an "interested person" may seek such an accounting.

At least one court has found that while a beneficiary had sufficient standing to bring a cause of action against the trustees, the contingent beneficiary did not have sufficient standing to seek an accounting because the contingent interest was insufficient to require an accounting. *Hill v. Hunt*, 2009 WL 5125085, No. 3:07-CV-2020-O at *7 (N.D. Tex. Dec. 29, 2009) (holding plaintiff had insufficient interest to demand accounting); see also *Hill v. Hunt*, 2009 WL 5178021, No. 3:07-CV-2020-O (N.D. Tex. Dec. 30, 2009) (holding plaintiff had sufficient interest to bring suit).

Note that the language of Tex. Prop. Code § 131.151 leaves open that the terms of a revocable trust may limit the duty to account. This is also addressed above in the section on revocable trusts.

5. Derivative suits by beneficiaries

Normally only the trustee has standing to bring suit on behalf of the trust. However, if a trustee fails or refuses to bring a suit, a beneficiary may have standing to bring a derivative suit on behalf of the trustee.

This issue often arises where a trustee has breached his duties, such as misappropriated trust funds, and obviously will not sue himself for such breach.

The leading Texas case on derivative causes of action is *Interfirst Bank-Houston, N.A. v. Quintana Petroleum Corporation,*[17] in which the court held that:

> It is the right and responsibility of the testamentary trustee to assure that all property willed into a trust is properly conveyed by the executors of the settlor's estate. It is only when the trustee cannot or will not enforce the cause of action that he has against the third person, that the beneficiary is allowed to enforce it.

The *Quintana* court relied on Bogert, *Trusts and Trustees (2nd Edition Revised)* § 869, which addresses derivative suits. Where a trustee cannot or will not bring a cause of action running to him for the benefit of

[13] *Id.* at *4.
[14] *Id*. at *4.
[15] *Id*. at 4.
[16] *Cote*, 2003 WL 23194260 at *4.
[17] 699 S.W.2d 864 (Tex. App. —Houston [1st Dist.] 1985, writ denied)

the beneficiary, the courts will vary their usual rules of standing. *Id.*

> There is danger that the cause of action may be barred by laches or the operation of the Statute of Limitations, if the beneficiary is obliged to wait for the trustee to act, or is forced to sue the trustee to compel action, or to bring a proceeding for the removal of the trustee and the appointment of a successor. In addition the financial condition of the third party may change so that all relief will be shut off.

A derivative suit may be brought where:

1) The trustee refuses to bring suit, after demand, or fails to act;
2) The trusteeship is vacant;
3) The trustee has been absent for many years;
4) The trustee has an adverse interest or has conspired to defeat the trust;
5) The trustee is held estopped to sue a third party;
6) The trustee cannot be subjected to the jurisdiction of the court.

Id.; Restatement of the Law of Trusts 2d § 282. When a derivative suit is brought, the trustee is made a party defendant. This is one of those situations where you must be clear with your client that the beneficiary is not enforcing his own claim but is acting as a temporary representative of the trust to effect a recovery. Any recovery will go to the trust estate for the benefit of the beneficiaries. *Id*.

IV. PERSONAL JURISDICTION

Texas Prop. Code § 115.011 requires a plaintiff to join "necessary parties" to a trust action, including the trustee(s) and certain beneficiaries, including: (1) a beneficiary of a trust on whose act or obligation the action is predication; (2) a beneficiary of the trust designated by name, other than a beneficiary whose interest has been distributed, extinguished, terminated or paid; (3) a person who is actually receiving distributions from the trust estate at the time the action is filed. A Texas court does not have jurisdiction over the matter if all of the "necessary parties" are not joined. *Estate of Bean*, 120 S.W.3d 914, 921 (Tex. App.—Texarkana 2003, pet. denied). Is it possible for a trustee or beneficiary to be a "necessary party" under Tex. Prop. Code § 115.011, but a Texas court not have personal jurisdiction over that necessary party because the party lives out of state? This section deals with personal jurisdiction over non-resident "necessary parties" in trust lawsuits.

A. Illustrations of how this issue may arise.

1. A trust is established while the settlor lives in Kansas. He was the beneficiary at the time the trust was established, but upon his death, all remainder beneficiaries live in Texas. One co-trustee lives in Texas, the other lives in New York. All relevant claims (misappropriation of funds by the Texas co-trustee) took place in Texas. The New York co-trustee has never been to Texas and has never participated in the administration of the Trust. Therefore, the New York co-trustee argues that he does not have such "minimum contacts" with Texas sufficient to establish personal jurisdiction to make him a party to the suit. Yet, such trustee is a "necessary party" to the action under § 115.011. All relevant causes of action took place in Texas, all witnesses are in Texas, the Plaintiff beneficiaries are all in Texas, and the primary defendant is in Texas.

Is it possible that Plaintiffs may not be able to sue in Texas because they cannot establish personal jurisdiction over all necessary parties in Texas?

2. A trust is established by settlor while living in Mississippi. Settlor was the original beneficiary, but he has died. The current beneficiaries all live in Texas and have lived there since the inception of the trust. The trust does not specify what state's law will apply. The three co-trustees live in Florida, New York and California, and they do not have any contacts with Texas, other than receiving requests for distributions from the current beneficiaries. The current beneficiaries are suing the co-trustees because they have not received any distributions.

Should those trustees be subject to personal jurisdiction in Texas?

3. Same facts as #2, but the current beneficiaries moved to Texas five years after the trust was created.

Should those trustees be subject to personal jurisdiction in Texas?

B. Overview of Jurisdiction:

1. <u>Service on a Non-Texas Defendant</u>

A nonresident can be effectively served if he is physically present in the state, unless (i) he has been fraudulently enticed to enter the state by the plaintiff for the purpose of being served, (ii) he comes to serve as a witness in a criminal case, or (iii) he has made a special appearance in the case.

Valid in-state service provides a Texas court with general jurisdiction – i.e., jurisdiction over the defendant's person and property for *all* claims.

2. <u>Personal Jurisdiction</u>

A Texas court may exercise personal jurisdiction over a nonresident defendant if: (1) the Texas long-arm statute authorizes the exercise of jurisdiction; and (2)

the exercise of jurisdiction is consistent with federal and state constitutional guarantees of due process. *Retamco Operating, Inc. v. Republic Drilling Co.*, 278 S.W.3d 333, 337 (Tex. 2009).

Personal jurisdiction over nonresident defendants is constitutional when: (1) the defendant has established minimum contacts with the forum state, and (2) the exercise of jurisdiction comports with traditional notions of fair play and substantial justice. *Id. at 338.* In deciding whether it is proper to call a non-resident defendant before a Texas court, the court focuses on the defendant's activities and expectations. *Id*. at 338.

To determine whether a plaintiff met their initial burden to plead sufficient allegations to invoke jurisdiction under the long arm statute, the court looks to the jurisdictional facts "pleaded in their petition, as well as the jurisdictional facts alleged in their response to [defendant's] special appearance." *Alencar v. Shaw*, 323 S.W.3d 548, 552 (Tex. App.—Dallas 2010, no pet.).

a. Minimum Contacts:

A state generally has a "manifest interest" in providing its citizens with a convenient forum for redressing wrongs inflicted by out-of-state actors. *Burger King v. Rudzewicz,* 471 U.S. 462, 473, 105 S.Ct 2174, 85 L.Ed. 2d 528 (1985). Where an individual purposefully derives benefit from his activity in another state, it may be unfair to allow him to escape having to account in another state for consequences that arise proximately from such activity. *Id*. at 473-74. A defendant cannot use the Due Process Clause as a territorial shield to avoid interstate obligations that he has voluntarily assumed. *Id*.

A court has personal jurisdiction over a nonresident defendant if his minimum contacts give rise to either general or specific jurisdiction. *BMC Software Belgium, N.V. v. Marchand,* 83 S.W.3d 789, 795-96 (Tex. 2002).

(1) General Jurisdiction:

General jurisdiction is present when a defendant's contacts in a forum are continuous and systematic so that the forum may exercise personal jurisdiction over the defendant, even if the cause of action did not arise from or relate to activities conducted within the forum state. *BMC,* 83 S.W.3d at 796.

(2) Specific Jurisdiction:

A Texas court may assert specific jurisdiction over a non-resident defendant if the defendant's contact with the state is purposeful and the injury arises from or relates to those contacts. *Retamco,* 278 S.W.3d at 338.

In a specific jurisdiction analysis, the court focuses on the "relationship among the defendant, the forum and the litigation." *Retamco*, 278 S.W.3d at 338. The minimum-contacts analysis is focused on the quality and nature of the defendant's contacts, rather than their number. *Retamco,* 278 S.W.3d at 339.

A non-resident defendant establishes minimum contacts with a state when it "purposefully avails itself of the privilege of conducting activities within the forum state, thus invoking the benefits and protections of its laws." *Retamco,* 278 S.W.3d at 338. The defendant's activities, whether they are direct acts within Texas or conduct outside Texas, must justify a conclusion that the defendant could reasonably foresee being called into a Texas court." *Id*.

A nonresident defendant that has "purposefully availed" itself of the privileges and benefits of conducting business in the foreign jurisdiction has sufficient contacts with the forum to confer personal jurisdiction. *BMC,* 83 S.W.3d, at 795.

Thus where a non-resident defendant has deliberately engaged in significant activities within a state, or has created "continuing obligations" between himself and residents of the forum state, he manifestly has availed himself of the privilege of conducting business there. *Burger King,* 471 U.S. at 475-476.

Because such defendant's activities are shielded by "the benefits and protections" of the forum state's laws, it is presumptively not unreasonable to require him to submit to the burdens of litigation in that forum as well. *Id*.

Although not determinative, foreseeability is an important consideration in deciding whether the non-resident defendant purposefully has established minimum contacts with Texas. *BMC,* 83 S.W.3d at *795.* "The foreseeability that is critical to due process analysis ... is that the defendant's conduct and connection with the forum State are such that he should reasonably anticipate being haled into court there." *Burger King,* 471 U.S. at 474.

b. Asserting personal jurisdiction comports with "fair play and substantial justice."

Once minimum contacts are established, either through general or specific jurisdictions, the court must consider these contacts in light of other factors to determine whether the assertion of personal jurisdiction would comport with "fair play and substantial justice." *Burger King*, 471 U.S. at 476.

The factors relevant to this analysis are: 1) the burden on the defendant; 2) the forum State's interest in adjudicating the dispute; 3) the plaintiff's interest in obtaining convenient and effective relief; 4) the interstate judicial system's interest in obtaining the most efficient resolution of controversies; and 5) the shared interest of the several States in furthering fundamental substantive social policies. *Burger King*, 471 U.S. at 477.

C. Case law on Personal Jurisdiction in the Trust Context.

1. *Hanson v. Denckla*, 357 U.S. 235 (1958).

In *Hanson*, the U.S. Supreme Court addressed the issue of whether a court has jurisdiction over a trust claim if a trustee and beneficiaries are "necessary parties" under a state statute, but those necessary parties are not residents of the forum state and do not have minimum contacts with the forum state to subject them to personal jurisdiction. The Court held that the forum state's court does not have jurisdiction over the trust proceeding, and any decision affecting the trust is void.

While living in Pennsylvania, the settlor in *Hanson* created a trust that was expressly subject to Delaware law and named a Delaware trustee. The settlor, who held an inter vivos power of appointment, was the life beneficiary. After moving to Florida, the settlor executed a power of appointment appointing $400,000 out of the trust to two new trusts. The same day, the settlor executed a will. Settlor died in Florida and his will was admitted to probate in Florida. The issue in the Florida court concerned the right to the $400,000. The will beneficiaries claimed that the $400,000 trust corpus, which was held in Delaware, passed under the residuary clause of settlor's will because the power of appointment was invalid. The Florida court agreed and invalidated the appointment of $400,000 to the new trusts.

Under Florida law, like Texas law, all trust beneficiaries and the trustees were "necessary parties" to the Florida proceeding because it involved a trust matter. The trustees of the trusts and several of the beneficiaries were not Florida residents and failed to appear in the case.

The U.S. Supreme Court held that the Florida court lacked personal jurisdiction over the Delaware trustee, which trustee held no office in Florida, transacted no business in Florida, and did not administer the trust in Florida, therefore it had no "minimum contacts" with Florida. As such, the Florida court could not determine, as it did, that the property passed through the will rather than through the trust.

According to the Supreme Court, the Florida court does not acquire jurisdiction over the trustee merely because Florida is the "center of gravity" of the controversy or the most convenient location for litigation. By making trustees "necessary parties" to a trust action, Florida law makes a trustee an *indispensable party* in a proceeding affecting the validity of a trust.

While nothing would prevent Florida from adjudicating the rights and liabilities of an executor, legatees and appointees over whom it had personal jurisdiction, the mere fact that the settlor and most of the appointees and beneficiaries were domiciled in Florida would not give the Florida courts personal jurisdiction over the non-resident trustee. Where Florida was without jurisdiction over the Delaware trustee or over the trust corpus held in Delaware, the Florida judgment invalidating the trust was reversed not only as to the nonresident trustee but also as to the parties over whom the Florida court did have jurisdiction. *Id*. at 254.

Important note regarding *Hanson*: *Hanson* is unique because the question was whether property passed under a trust or a will, rather than being a pure trust lawsuit. In fact, it originated in a probate proceeding. Thus, *Hanson* should not be seen as a black and white rule that a court never has personal jurisdiction over non-resident trustees or beneficiaries. Personal jurisdiction determinations are made on a case-by-case basis. While *Hanson* is very useful, the following cases are perhaps more clear in how personal jurisdiction applies in a typical trust case.

2. *Dugas Ltd. Partnership v. Dugas*, 341 S.W.3d 504 (Tex. App.—Fort Worth 2011, pet. granted, judgm't vacated w.r.m.).

Dugas is incredibly instructive because the court held that it had personal jurisdiction over the non-resident trustees of Trust 1, however, it did not have jurisdiction over the non-resident trustee of Trust 2. Significantly, the non-resident trustee of Trust 2 was also one of the trustees of Trust 1. The logic behind the different conclusions lies in the facts surrounding the establishment of the trusts by the same settlor, which led to the creation of the non-resident trustees' minimum contacts, or lack thereof, related to the specific trusts.

The court found personal jurisdiction over the non-resident trustees of Trust 1. Trust 1 was executed when the settlor-beneficiary was a resident of Texas, a fact the co-trustees knew at that time. The court found personal jurisdiction over the co-trustees of Trust 1 because the co-trustees purposefully created ongoing obligations between themselves and the Texas beneficiary when they agreed to become co-trustees of Trust 1. The co-trustees made numerous distributions to the beneficiary during his lifetime, and each co-trustee could have reasonably anticipated being hailed into a Texas court to defend against the parties' claims arising from or relating to those contacts.

The court did not find personal jurisdiction related to Trust 2 because that trust was created *before* the settlor-beneficiary was a resident of Texas, and distributions made to the beneficiary while he lived in Texas were made only as a result of the beneficiary's unilateral act of moving to Texas several years after the creation of the trust. The trustee did not voluntarily undertake continuing obligations for the benefit of a Texas resident.

To find personal jurisdiction over a non-resident trustee in this situation, the *Dugas* court required:

- Beneficiary must be resident of the forum state at the time the trust is executed and the trustee agrees to accept the trust
- Trustee undertakes continuing obligations for benefit of a Texas resident

Persuasive Evidence Showing Minimum Contacts:

- Trustee makes trust disbursements to beneficiary in the forum state
- Terms of trust require trustee to make ongoing determinations regarding amount of distributions to make to beneficiary regarding health, education, maintenance and support, which necessarily requires regular contact with Texas

Reasoning:

- As a trustee, one voluntarily takes on the responsibility of administering a trust established for the benefit of a resident of Texas, and by entering into this agreement, which has a substantial connection to Texas, it is foreseeable that the trustee may be brought before a Texas court in Texas. See *Seijo v. Miller,* 425 F.Supp.2d 194, 200 (D.P.R.2006).

3. *Seijo v. Miller*, 425 F. Supp.2d 194, 200 (D.P.R. 2006)

Cited by *Dugas* as persuasive authority, the *Seijo* court in Puerto Rico found specific jurisdiction over two nonresident trustees. The defendants were trustees of a trust established in Louisiana for the benefit of a resident of Puerto Rico when trust was executed. The beneficiary received several trust disbursements while in Puerto Rico and litigation arose out of defendants' actions in administering the trust (defendants did not make proper disbursements to the beneficiary).

D. How Can Texas Make Personal Jurisdiction Easier for Practitioners?

The Uniform Trust Code (2010 Rev.) § 202 addresses the issue of personal jurisdiction over non-resident trustees and beneficiaries, and it may be advisable for Texas to adopt this provision to help clear up personal jurisdiction in Texas.

The UTC § 202 States: Personal Jurisdiction over trustee and beneficiaries:

(A) By accepting the trusteeship of a trust having its principal place of administration in this state or by moving the principal place of administration to this state, the trustee submits personally to the jurisdiction of the courts of this state regarding any matter involving the trust.

(B) With respect to their interests in the trust, the beneficiaries of a trust having its principal place of administration in this state are subject to the jurisdiction of the courts of this state regarding any matter involving the trust. By accepting a distribution from the trust, the recipient submits personally to the jurisdiction of the courts of this state regarding any matter involving the trust. (emphasis added)

(C) This section does not preclude other methods of obtaining jurisdiction over a trustee, beneficiary or other person receiving property from the trust.

The Comments to UTC § 202 provide that "the jurisdiction conferred over the trustee and beneficiaries in this section does not preclude jurisdiction by courts elsewhere on some other basis." The fact that a court in a new state acquires personal jurisdiction under this section after a change in a trust's principal place of administration does not necessarily mean that the courts of the prior principal place of administration lose jurisdiction, especially as to matters regarding events occurring before the transfer.

This section confers limited jurisdiction. *Id*. Subsection (b) states that until *a distribution is made*, jurisdiction over a beneficiary is limited to only the beneficiary's interests in the trust. *Id*. Personal jurisdiction over a beneficiary is conferred only upon a beneficiary accepting a distribution. *Id.* Subsection (b) does give the court jurisdiction over other recipients of distributions, which include individuals who mistakenly receive distributions. *Id*.

While UTC § 202 does not cure all personal jurisdiction issues (i.e. it does not grant personal jurisdiction over beneficiaries until they have received a distribution, thus it does not cover all "necessary parties"), this provision would further the cause in clarifying Texas law when personal jurisdiction may be exercised in trust causes of action.

Conclusion:

The issue of personal jurisdiction over non-resident trustees and beneficiaries who are necessary parties in a trust proceeding is a complicated matter. For more extensive coverage, see the following resources:

Scott on Trusts (4th ed. 1989) § 565-573 (particularly §§ 568, 571).

Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, S.Ct. 653, 94 L.Ed. 865 (1950);
Cocke v. Duke University, 260 N.C. 1, 131 S.E.2d 909 (1963).