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WHAT IS THE EFFECT OF TRUST LANGUAGE DESIGNED TO INSULATE THE TRUSTEE FROM LIABILITY?

When a lawyer drafts a trust instrument, the lawyer often will try to insulate the trustee from liability by giving the trustee “absolute,” “sole,” “uncontrolled,” or “unfettered” discretion. Or the lawyer may try to bar suits against the trustee on some issues, or for anything short of “willful misconduct.” This kind of exculpatory language seems inherently inconsistent with the system of accountability inherent in a trust relationship. What is the effect of such exculpatory language under Missouri trust law?

The question of whether a trustee breaches its fiduciary duty depends on the facts of the case. But this article addresses what happens when a beneficiary is faced with trust language designed to insulate the trustee from liability – regardless of the facts. The beneficiary may create a justiciable controversy on two possible theories: First, words of absolute discretion conferred upon a trustee will not insulate the trustee from liability when the trust supplies an objective standard and the trustee acts beyond the bounds of reasonable judgment. Second, the Missouri Uniform Trust Code provides that exculpatory trust language is unenforceable to the extent a beneficiary is able to prove that the trustee breached its trust in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries. See, §456.10-1008 RSMo (Cum. Supp. 2014).

I. Words of absolute discretion will not insulate the trustee from liability when (1) the trust contains an ascertainable support standard and (2) the trustee acts beyond the bounds of reasonable judgment.

Words of “absolute,” “sole,” or “uncontrolled” discretion in a trust instrument will not insulate the trustee from liability for failure to use its

good faith judgment in addressing an ascertainable standard. *O’Riley v. U.S. Bank*, 412 S.W.3d 400, 407 (Mo.App. W.D. 2013), citing §456.9-814.1 RSMo (Cum. Supp. 2012). “Where... a trust supplies a standard by which the reasonableness of a trustee’s judgment can be tested, a court will control the exercise of a power when it acts beyond the bounds of reasonable judgment.” *O’Riley*, 412 S.W.3d at 406.¹ In the end, the Western District in *O’Riley* affirmed a judgment in favor of the trustee. In doing so, however, the court disregarded words of absolute discretion in the trust instrument and applied the standard of whether the trustee acted beyond the bounds of reasonable judgment in making distribution decisions. *Id.* at 411.

More than two decades ago, the Southern District explained the limits of a trustee’s discretion when the grantor supplies a standard by which to test the reasonableness of the trustee’s judgment. See, *Heisserer v. Friedrich*, 797 S.W.2d 864, 870 (Mo.App. S.D. 1990). In such circumstances, the court “will control the trustee in the exercise of a power when he acts beyond the bounds of reasonable judgment.” *Id.* at 870. The Southern District applied this principle to reject the trustees’ argument that they had unlimited, unfettered discretion to sell a farm. The trustees relied on a trust clause purporting to give them “absolute discretion” to sell the farm for the benefit of the settlor and her daughter. The Southern District rejected this claim because the trustees had not shown a convincing need for sale. Contrary to their view, the Southern District held that neither the applicable trust statutes nor the term of the trust indenture “vest the trustees with the unlimited, unfettered discretion for which they contend.” *Id.* at 872.²

A trust typically will supply an objective standard by calling on the trustee to distribute income or principal for the “health, education, support and maintenance” of one or more beneficiaries. This kind of clause is universally recognized in trust law as an ascertainable standard for support. See, *Lanagan v. Rorke*, 182 S.W.3d 596, 601 (Mo.App. S.D. 2005) (where appellant conceded such language created an ascertainable standard). So, even if the trust purports to give the trustee absolute discretion in making

¹ The court suggested the reasonable judgment standard draws its origins from *The Restatement (Second) of Trusts* §187, comment i, and *The Restatement (Third) of Trusts* §50, comment b.

² The Western District reaffirmed the vitality of the *Heisserer* reasoning by applying the holding to a similar set of facts in *Betty G. Weldon Revocable Trust v. Weldon*, 231 S.W.3d 158, 175-77 (Mo.App. W.D. 2007).

distributions, the trustee still should be bound by the reasonable judgment test.

II. Exculpatory trust language is unenforceable if the plaintiff is able to prove that the trustee breached its trust in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries.

The Missouri Uniform Trust Code provides another possible basis for avoiding exculpatory language in the trust. Under §456.10-1008 RSMo (Cum. Supp. 2014), the term of any exculpatory clause in a trust is unenforceable “to the extent that it...relieves the trustee of liability for breach of trust committed in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries....”³

This section of the Missouri Uniform Trust Code was enacted in 2004. Because the law is still relatively new, no Missouri appellate court appears to have construed this particular section. Yet other jurisdictions have addressed this same part of the uniform code. For instance, the Kansas Court of Appeals applied the statute to reverse summary judgment in favor of a trustee. *Schwartz v. Barker*, 291 P.3d 1073, 2013 Kan. App. Unpub. LEXIS 37 at *32-33 (Ks. Ct. App. January 11, 2013) (finding a genuine dispute over whether the trustee breached his fiduciary duties in bad faith or in conscious disregard of potential harm to the interests of the beneficiaries). On the other hand, an Ohio appellate court affirmed a judgment absolving a trustee from liability under the statute because of findings that the trustee had not acted in bad faith, willful default or with reckless indifference to the purposes of the trust. *Newcomer v. National City Bank*, 19 N.E.3d 492, 504-05 (Ohio Ct. App. 2014).

The ultimate question under the statute is whether the plaintiff can prove that the trustee acted in bad faith or with reckless indifference. If so, the exculpatory language will not save the trustee from liability.

³ This Missouri Code section codifies the public policy concerns about exculpatory clauses under the common law. See, e.g., *Vena v. Vena*, 387 Ill.App.3d 389, 397-99, n. 4 (Ill. App. Ct. 2nd Dist. 2008), citing *The Restatement (Second) of Trusts*, §222(2), at 516 (1959) (“Illinois law is clear that the trust instrument cannot entirely insulate the trustee from court review of his or her actions.”)

III. Conclusion

This article is not intended to draw any conclusions about whether the trustee breaches its fiduciary duty under any particular set of facts. But a beneficiary should not necessarily give up on a legitimate claim against a trustee just because the language of the trust appears to bar the lawsuit. Regardless of such exculpatory language, the plaintiff still may have a valid claim if the facts show that the trustee acted beyond the bounds of reasonable judgment. And the Missouri Uniform Trust Code makes the exculpatory language unenforceable if it can be shown that the trustee acted in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries.

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