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Trustees Beware

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In light of new Florida legislation on Trust Administration effective as of July 1, 2008, Trustees now, more than ever, should be aware of their obligations to avoid potential misstep leading to liability. This article highlights a Trustee's basic duties and issuance of the new rule on the payment of costs or attorney's fees from Trust assets.

Generally, the administration of a Trust is free from judicial intervention and proceeds without order, approval or action of any court, unless the court is called upon by interested parties to resolve a disputed matter. Otherwise, obligations, management and distribution of a Trust estate proceed in accordance with the terms of the Trust.

Trustees must file U.S. Income Tax Return for Estates and Trusts (IRS Form 1041) if the Trust contains income in excess of \$600.

Trustees must use due care, diligence and prudence in administering a Trust for the benefit of the beneficiaries. This includes a duty to treat all beneficiaries equally and to protect their individual interests in the Trust with the same degree of care that a reasonably prudent person would exercise under similar circumstances. If the duty of a Trustee and individual interest of a Trustee conflict, then the power of a Trustee may only be exercised with court authorization.

Furthermore, Trustees have a duty to invest and manage investment assets as a prudent investor would, considering the purposes, terms, distribution requirements and other circumstances of the Trust. Investment decisions or actions will be considered in the aggregate, under the facts and circumstances prevailing at the time of the decision of action. No specific incident, considered in isolation, is prudent or imprudent. The prudent investor rule is a test of conduct, not one of resulting performance. Trustees have the ability to delegate any part or all of the investment functions that a prudent investor of comparable skills might delegate under the circumstances to an investment agent.

Trustees have a duty to keep the beneficiaries of a Trust reasonably informed of the Trust and its administration, which includes, within 60 days after acceptance of the Trust, informing the qualified beneficiaries in writing of the acceptance of the Trust and the full name and address of the Trustee. Upon request of a qualified beneficiary, Trustees must provide a complete copy of

the Trust instrument, including any amendments, and relevant information about the Trust assets and the particulars relating to administration. Because qualified beneficiaries are entitled to an annual trust accounting, Trustees must keep a complete records of all transactions. This requires that an opening inventory of the assets and liabilities and records be maintained, showing all principal and income receipts, disbursements and distributions.

Annual Trust accountings must be a reasonably understandable report, prepared by Trustees, unless the beneficiaries have waived their right to receive these reports. A Trust accounting is required to adequately disclose the following information:

- A statement identifying the Trust, the Trustee and the time period covered by the Trust accounting.
- All significant transactions affecting the Trust during the accounting period, including compensation paid to the Trustee and the Trustee's agents, all cash and property transactions, gains and losses realized and all receipts and disbursements.
- Identity and value of Trust assets on hand at the close of the accounting period, including both the asset acquisition value (carrying value) and the estimated current value. Identity of each non-contingent liability and the estimated current amount of liability, if known.
- Significant transactions that do not affect the amount of the Trust, such as name changes in investment holdings, adjustments to carrying value, change of custodial institutions and stock splits.
- Allocation of receipts, disbursements, accruals or allowances between income and principal when allocation affects the interest of any beneficiary of the Trust.

Furthermore, Trustees should include a limitation notice (preferably in the annual accounting), informing beneficiaries as to the time period in which an action for breach of Trust based on matters disclosed in a Trust accounting or other written reports may be maintained. If a limitation notice is properly sent to a beneficiary, the beneficiary has only **six (6) months** in which to bring a cause of action against the trustee for any transactions enclosed in the trust accounting. If the limitation notice is not properly sent to the beneficiary with the trust accounting, the beneficiary has up to **four (4) years** to bring a cause of action against the trustee for any action taken by the trustee that is adequately disclosed to the beneficiary. Therefore, in order to limit your liability exposure, it is imperative that trust accountings and limitation notices be sent to the beneficiaries in accordance with Florida Law.

Trustees have always had the duty to act reasonably in relation to the expenses of Trust administration and, traditionally, Trustees have had the ability to make payment of costs or attorney's fees incurred in any trust proceeding (including an action against the Trustee) from the assets of the Trust without approval of any person or authorization of the court. Yet under newly enacted law, Trustees may not be able to use the trust assets to pay for costs relating to their defense in a breach of trust cause of action.

If a claim or defense based upon a Trustee's breach of Trust is made against a Trustee, the Trustee must provide written notice to each qualified beneficiary of the Trust whose share of the Trust may be affected by these payments, informing them of the intention to make payments from the Trust **prior** to making payment. This written notice must include notice of the right to apply to the court for an order prohibiting the Trustee from paying costs or attorney's fees from Trust assets.

If the court concludes that there is a reasonable basis to find a breach of Trust, unless the court finds the breach to be a result of good cause, an order prohibiting payment will be entered. If the order is entered once payment has already been made from the Trust, further payment is precluded and payment previously made must be refunded to the Trust. Thus, the Trustee could have to pay attorney's fees and costs out of his or her own pocket.

The upside? Following a final determination of the claim or defense based on breach of Trust by the court, Trustees may seek an order permitting the payment of some or all costs or attorney's fees incurred in the proceeding. Also, if this claim or defense is withdrawn, dismissed or resolved prior to the court's determination, Trustees are free to make payments from the assets of the Trust without further court authorization. However, until there is a final determination or until the claim is withdrawn, the Trustee must pay for the expenses out of pocket. Trust proceedings can take years to come to a conclusion, so even if the Trustee eventually gets reimbursed from the Trust, the Trustee can face a heavy financial burden while the case is pending.

The good news for Trustees is that they are entitled to reasonable compensation for their services. What reasonable compensation is depends on the circumstances involved in the trust administration.

Your compliance with the laws of the State of Florida pertaining to Trustees' duties and powers is imperative to avoid liability as a Trustee. If you have any questions concerning your obligations as a Trustee or if specific issues should arise during the administration of the Trust, we encourage you to contact us.

Note: this article is intended to provide an overview of a Trustee's duties and responsibilities only, and is not intended to provide specific or comprehensive legal or tax advice

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About Dean Mead:

Dean Mead is a commercial law firm that provides full-service legal representation to businesses and individuals throughout Florida. The firm has close to 50 lawyers practicing in Orlando, Fort Pierce and Viera.