

Exculpatory Clauses in *Inter Vivos* Trusts: What Remains of a Trustee's Duty of Undivided Loyalty?

By Ian W. MacLean

I. Introduction

In the State of New York, exculpatory clauses in trusts, whether testamentary or *inter vivos*, are common. Exculpatory clauses in trusts are those provisions intended to limit or eliminate the liability of a trustee resulting from the trustee's breach of the fiduciary duty of an undivided loyalty to the beneficiaries of a trust.¹

Notwithstanding what may be the most eloquently articulated standard of fiduciary responsibility in our nation's jurisprudence,² our laws have evolved to permit testators of wills creating trusts and grantors of *inter vivos* trusts certain latitude in exonerating their trustees from liability caused by the trustee's breaches of the trustee's duty of undivided loyalty to the trust and its beneficiaries. There is a significant difference, however, in the rules governing exculpatory clauses in wills and testamentary trusts and those governing such clauses in *inter vivos* trusts: the validity of exculpatory clauses in wills and testamentary trusts is governed by Estates, Powers and Trusts Law 11-1.7; there is no separate statutory provision for exculpatory clauses in *inter vivos* trusts, which EPTL 11-1.7 omits.³

In all but a very few cases, which are discussed herein, New York courts have declined to apply EPTL 11-1.7 to exculpatory clauses in *inter vivos* trusts. This article discusses the rules governing exculpatory clauses in *inter vivos* trusts and raises the issue of whether the New York legislature should establish a standard by which exculpatory clauses in *inter vivos* trusts should, quite literally, be judged.

II. "The Standard of Behavior"

Under New York law, a trustee owes a duty of undivided loyalty to the beneficiaries of the trust for which the trustee serves.⁴ Since at least the late nineteenth century, the Court of Appeals has rearticulated this rule time and time again, in what may be characterized as an ongoing effort to get the message through.⁵

For example, in 1886, in *Munson v. Syracuse, Geneva & Corning RR Co.*,⁶ the Court opined that a contract signed by a trustee who is personally inter-

ested in the subject of the sale of trust assets "is repugnant to the great rule of law which invalidates all contracts made by a trustee or fiduciary, in which he is personally interested." Over a half-century later in 1951, in *In re Hubbell's Will*,⁷ the Court of Appeals made abundantly clear that "[i]n judging the conduct of trustees, the basic consideration is the fiduciary obligation which they owe to all of the beneficiaries whom they represent."⁸ And during the intervening sixty-five years the Court ruled on the standard of a trustee's fiduciary duty several more times.⁹ In *Meinhard v. Salmon*,¹⁰ Chief Judge Benjamin N. Cardozo set forth what is perhaps the best known and most relied on articulation of a trustee's duty—"the standard of behavior":

The Trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.¹¹

Given such language, it would seem that *Meinhard* left little doubt, if any, of the standard to which a trustee must adhere.

III. Exceptions to the Standard

Nevertheless, that a grantor may exonerate his or her trustee from certain breaches of this undivided loyalty has survived under New York law. *Crabb v. Young*,¹² decided nearly a half-century before *Meinhard*, serves as a starting point. In *Crabb*, the exculpatory clause protected the trustees from liability for any loss except for that arising from their "own will-

ful default, misconduct or neglect.”¹³ Lacking any evidence of such willful conduct, the Court held that it was an error to hold the trustees liable for loss resulting from their management of the trust, even though they had acted imprudently.¹⁴

In an opinion by Chief Judge William C. Ruger, the Court attempted to balance the fiduciary duty of a trustee against what was decidedly the grantor’s desire to insulate his trustee from certain liability. On the one hand, the Chief Judge opined that, as the testator “knew well the character and qualifications” of his selected trustees (some of his children), he had an “absolute right to . . . impose the terms and conditions” under which his trustees would serve, and the Court had no right to increase the measure of the trustees’ responsibility by imposing a higher standard, absent willful or fraudulent misconduct.¹⁵

Trusts of property are generally created for the benefit and support of the young, helpless and inexperienced and depend largely for their proper administration upon the honesty and capacity of those to whom they are confided. . . . [T]he court will guard their rights with jealous care and scrutinize closely the conduct of trustees with the view of holding them to a high degree of responsibility in the management and control of trust estates. But while trustees are thus held to great strictness in their dealings with the interests of their beneficiaries, the court will regard them leniently when it appears they have acted in good faith, and if no improper motive can be attributed to them, the court have even excused an apparent breach of trust, unless the negligence is very gross.¹⁶

While the legislature eventually saw fit to void the right of a testator to exonerate his or her trustee from liability for a failure to act in accordance with a duty of undivided loyalty,¹⁷ it imposed no such limitation on grantors of *inter vivos* trusts. Over time, the courts of New York have embraced and cultivated the principles in *Crabb* set forth above into a set of standards that are far less restrictive and permit exculpatory clauses to relieve a trustee from liability in the absence of a showing of willful negligence, self-dealing or bad faith.¹⁸

In *O’Hayer v. de St. Aubin*,¹⁹ an oft-cited case in this area, the Appellate Division set forth the rule

governing the validity of exculpatory clauses in *inter vivos* trusts as follows:

No matter how broad the [exculpatory] provision may be, the trustee [of an *inter vivos* trust] is liable if he commits a breach of trust in bad faith or intentionally or with reckless indifference to the interest of the beneficiaries, or if he has personally profited through a breach of trust.²⁰

In *O’Hayer*, the grantor named himself, his son and three others as co-trustees of a trust. The trust held stock in the grantor’s closely held business. The exculpatory provisions of the trust provided as follows:

Although it may be a general rule of law that a trustee shall not profit from his trusteeship, I expressly declare and direct that this rule shall be completely ignored and set aside in the administration, construction and interpretation of this trust in so far as it could relate to or affect or be applied to my trusteeship or the trusteeship of my son hereunder. . . .²¹

In addition, the trustees were granted broad powers “far beyond the traditional notions of trusteeship,”²² including the right to purchase assets from the trust for themselves and to profit from their relationship as trustees of the trust, which they did.²³ After the grantor’s death, his daughter—the remainder beneficiary—challenged her trustee-brother’s right to purchase shares of the corporation’s stock and demanded an accounting by the trustees.²⁴

With an almost perfunctory reference to the seminal Court of Appeals cases of *Meinhard v. Salmon*,²⁵ *Dutton v. Willner*²⁶ and *Munson v. Syracuse, Geneva & Corning R.R. Co.*²⁷ for the proposition that a trustee owes a duty of undivided loyalty to the trust, the *O’Hayer* court opined that, without a doubt, “the rule of undivided loyalty due from a trustee may be relaxed by a grantor of a trust by appropriate language in the trust instrument in which he, either expressly or by necessary implication, recognizes that the trustee may have interests potentially in conflict with the trust.”²⁸

As if to bolster this point, the *O’Hayer* court continued, “at least, our courts under these conditions enforce the desire of the settlor to secure the services of a person to act as trustee in whom he has confidence, when, without the existence of exculpatory

provisions, the trusteeship would be declined by the designee."²⁹

The most troubling aspect of this part of the court's reasoning is that only one of the cases cited, *In re Balfe*, stands directly for this proposition.³⁰ Furthermore, while *Crabb* and its progeny support the proposition that a grantor may explicitly exculpate a trustee from certain acts or omissions, nowhere in *Crabb* does the Court of Appeals provide any support for the proposition that a court may *infer* a grantor's intent to exculpate his or her trustee from liability for violating the duty of undivided loyalty to the beneficiaries of the trust.³¹

The *O'Hayer* court did recognize that regardless of the exculpatory language in a trust, New York law requires that a trustee "always exercise good faith in his administration" of the trust; exculpatory "directions" of a settlor do not allow a trustee "free rein" in dealing with the trust.³² Moreover, the court opined that any exculpatory language shall be strictly construed so that a "trustee's action will not be approved if he trespasses outside the boundaries of the powers granted" in the trust.³³ Nevertheless, the *O'Hayer* court seemed to give somewhat short shrift to the significance of the requirement that exculpatory language must be strictly construed, a principle that dates back at least to the beginning of the twentieth century.³⁴

In *In re Mallon's Estate*, for example, a case involving a testamentary trust with two trustees, trustee one, knowing that trustee two owed the estate over \$30,000, transferred the deed to an income-producing real property asset from the trust to trustee two. The exculpatory language in the will exempted a trustee "from liability for losses occurring without his own willful default."³⁵ The Appellate Division held that the conveying trustee had intentionally disregarded the rules that a prudent man would have followed in managing his own business affairs and was, therefore, liable to the beneficiary for the loss.³⁶

The *O'Hayer* court concluded that, as a rule, a trustee was liable for a breach in his duty of undivided loyalty to the trust, regardless of an exculpatory clause to the contrary, if his breach was in bad faith or with intentional or reckless disregard for the interests of the beneficiary.³⁷ In the end, the *O'Hayer* court held that the brother as trustee benefited from his manipulation of the company funds, of which the trust owned a considerable share; he failed to put the beneficiary's interests before his own; he had violated the covenant of good faith and thus his fiduciary duty; and was therefore liable to his sister for the loss.³⁸

IV. Contemporary Developments

In the course of the past two decades, it has become apparent that at least some of the Surrogates of New York are struggling with upholding exculpatory clauses in *inter vivos* trusts. Some Surrogates have gone so far as to suggest that EPTL 11-1.7 should apply to *inter vivos* trusts and at least two have actually applied the principles of the statute to lifetime trusts.

In *In re Helen R. Scheuer*, Surrogate Preminger (New York County) opined that exculpatory language will not necessarily absolve a trustee from liability for egregious self-dealing.³⁹ *Scheuer* involved an *inter vivos* trust, a family partnership, loans, lines of credit and unlimited personal guarantees. The exculpatory language in the trust provided that no trustee "shall be responsible or liable . . . for any act or omission of any other Trustee, or, unless his conduct amounts to bad faith and intentional and willful misconduct, for any act of omission of his own."⁴⁰

Starting from the premise that "fiduciaries who place their beneficiaries at financial risk in order to further their own objectives are deemed to breach their fiduciary duties,"⁴¹ the court held that "[i]n appropriate circumstances, a fiduciary can be held liable for his own acts and omissions and/or for the acts and omissions of his co-fiduciaries, despite purportedly exculpatory language in the governing instruments."⁴² However, because the Surrogate was ruling on a motion to dismiss for failure to state a cause of action, she did not reach the issue whether the exculpatory provisions in Mrs. Scheuer's trust absolved the trustee from liability in that case.⁴³ Thus, it is not clear that Surrogate Preminger extended the general rule to the alleged "egregious self-dealing" of the Scheuer fiduciaries.

In *In re Wasserman*,⁴⁴ the trust language extended the trustees' powers after the termination of the trust until all of the trust assets were distributed. The trustees retained assets two years after the trust terminated and the beneficiaries sued for losses incurred by the retention of the assets. Notwithstanding the exculpatory language that afforded the trustees "broad latitude to make and retain investments not ordinarily considered suitable for trustees under usual fiduciary investment standards,"⁴⁵ Surrogate Riordan held that the retention of trust assets for a period exceeding two years after the termination of the trust was unreasonable.⁴⁶

The Surrogate opined that "[w]hile there is a developing convergence, the law does continue to recognize a distinction between exculpatory provi-

sions in a Will as opposed to an *inter vivos* trust.”⁴⁷ Moreover, according to the Surrogate, “[t]he restrictions grounded in public policy contained in EPTL 11-1.7 do not apply to the trustee of a lifetime trust whose grantor can set the standards.”⁴⁸

In *Bauer v. Bauernschmidt*,⁴⁹ the provisions of an *inter vivos* trust provided that the trustee “was not to be held liable for any act or failure to act where he acted in good faith.”⁵⁰ The Appellate Division held that “exculpatory provisions like those in the present case are valid in *inter vivos* trust so long as there is some accountability, at least to the settlor.”⁵¹ While the *Bauer* court never cited to EPTL 11-1.7 or opined on whether the statute applies to *inter vivos* trusts,⁵² the court did find that capital expenditures of \$2,500 the trustee made from the trusts, and from which the trustee personally profited, constituted an improper appropriation of trust property for which the trustee was liable.⁵³

In *In re Mede*,⁵⁴ a case involving the establishment of an *inter vivos* trust for the benefit of minors who were to receive the proceeds of a personal injury/wrongful death case, the Surrogate did cite to EPTL 11-1.7. The draft trust proposed to the court contained language absolving the trustee “for his failure to use reasonable care or even ‘best efforts’ in choosing” appropriate investments.⁵⁵ Surrogate Feinberg acknowledged that EPTL 11-1.7 makes it contrary to public policy to exonerate executors and testamentary trustees for “failure to exercise reasonable care, diligence and prudence.” Nevertheless, the Surrogate held that, even though the trust at bar was an *inter vivos* trust, “the exonerating provisions in the [trust] clearly violates public policy as well as the standard of care established for fiduciaries [under New York law].”⁵⁶

The provision of the supplemental needs trust in *In re Goldblatt*⁵⁷ exonerated the trustee from liability for “any act or omission . . . except as to gross negligence, willful neglect or unlawful act[s].”⁵⁸ In striking the provisions from the proposed *inter vivos* trust, Surrogate Radigan relied directly and exclusively on EPTL 11-1.7 for the proposition that “it is contrary to public policy to exonerate a fiduciary from liability for failure to exercise reasonable care, diligence and prudence.”⁵⁹

Correspondingly, in *In re Amaducci*,⁶⁰ the trustees of an *inter vivos* trust were alleged to have pledged or loaned trust assets to entities in which the trustees held an ownership interest. Surrogate Emanuelli relied explicitly on EPTL 11-1.7 in holding that the beneficiaries claims of negligence, self-dealing and breach of fiduciary duty by the trustees were suffi-

cient to survive a motion to dismiss for failure to state a cause of action, notwithstanding an exculpatory clause that exonerated the trustees from liability for *any decision* made under the discretionary powers granted under the trust instrument.⁶¹

Similarly, Surrogate Riordan, in *In re Kassover*,⁶² and the Appellate Division, Third Department, in *In re Malasky*,⁶³ have held that the provisions in an *inter vivos* trust excusing the trustee from a duty to account to anyone is against public policy.

Finally, on the procedural level, in at least one case the Appellate Division has affirmed the decision of a trial court granting a motion to dismiss objections to an accounting on the ground that the beneficiaries failed to allege acts of actual bad faith or purposeful malfeasance sufficient to overcome an exculpatory clause in a voting trust.⁶⁴ Therefore, as with so many objections in an accounting, it is critical for the aggrieved party to allege sufficient acts or omissions of bad faith, purposeful malfeasance, reckless indifference to the interest of the beneficiaries, or personal profiting by the trustee.

V. Conclusion

As one pair of commentators forecast,⁶⁵ it appears that different standards are emerging among the various courts of New York State. In certain courtrooms, exculpatory clauses that purport to exonerate a trustee from a breach of the trustee’s duty of an undivided loyalty to the beneficiaries of an *inter vivos* trust may be upheld but only so long as the violation is not in bad faith or with intentional or reckless disregard for the interests of the beneficiary, or one from which the trustee profited. In other courtrooms, certain exculpatory clauses, such as those that purport to excuse a trustee from using reasonable care or the trustee’s best efforts, may be held invalid under certain facts and circumstances. And in yet other counties, exculpatory clauses in *inter vivos* trusts may be held void as against public policy as if the standard and principles of EPTL 11-1.7 apply. Such inconsistency in the contemporary decisions of the trial courts creates an unacceptable and undesirable level of uncertainty for both attorney and client in determining whether or how to use exculpatory clauses in *inter vivos* trusts.

A solution is needed. The legislature could amend EPTL 11-1.7(a) to include *inter vivos* trusts (by deleting the word “testamentary”); this may be too restrictive. Perhaps New York should adopt the approach of the Restatement (Second) of Trusts or that of the Uniform Trust Code. Or perhaps we should continue the dichotomy between testamen-

tary and *inter vivos* trusts by encouraging the legislature to enact a new statute that permits a grantor to provide some additional protection for the trustee while ensuring that the trustee's duty of an undivided loyalty does not fall prey to "the 'disintegrating erosion' of particular exceptions."⁶⁶ Whatever the solution, it is time for thoughtful discussion on this topic in and among the appropriate committees of the state and local bar associations, which, hopefully, will result in direction from the legislature.⁶⁷

Endnotes

1. "A true exculpatory provision is really one which relieves the trustee from liability for performing an act, which in the absence of the provision would make him liable." Fourth Report of the Temp. State Comm'n on the Modernization, Revision and Simplification of the Law of Estates, N.Y. Leg. Doc. No. 19, at 500 (May 31, 1965) ("1965 Commission Report").
2. *E.g.*, *Meinhard v. Salmon*, 249 N.Y. 458, 464, 164 N.E. 545, 546, 62 A.L.R. 1 (1928).
3. Section 11-1.7 of the Estates, Powers and Trusts Law ("EPTL") invalidates as against public policy any attempt to exonerate an executor or testamentary trustee "from liability for failure to exercise reasonable care, diligence and prudence." EPTL 11-1.7(a)(1) (McKinney's 2001 & Supp. 2004). In response to the Appellate Division decision in the once-famous case *In re Curley's Will*, 151 Misc. 664, 272 N.Y.S. 489 (N.Y. Surr. Ct. 1934), modified, 245 A.D. 255, 280 N.Y.S. 80 (2d Dep't), *aff'd without opinion*, 269 N.Y. 548, 199 N.E. 665 (1935), the legislature enacted the precursor to EPTL 11-1.7, Decedent Estate Law § 125 in 1936. *See* N.Y. Laws 1936, c.378 (May 2, 1936).
For a discussion of *In re Curley's Will* and the history behind the enactment of Decedent Estate Law § 125, see Note, *Legislation*, 6 Brooklyn L. Rev. 89 (1936) ("*Legislation*"); *see also* 1965 Commission Report, at 499–501. For a discussion of exculpatory clauses in trusts before the enactment of Decedent Estate Law Section 125, *see generally* Henry A. Shinn, *Exoneration Clauses in Trust Instruments*, 42 Yale L.J. 359 (1931) and Philip M. Payne, *Exculpatory Clauses in Corporate Mortgages and Other Instruments*, 19 Cornell L.Q. 171 (1934) (both cited in *Legislation*).
4. *E.g.*, *In re Donner*, 82 N.Y.2d 574, 584, 626 N.E.2d 922, 926, 606 N.Y.S.2d 137, 141 (1993) (and the cases cited therein).
5. Other New York courts have earlier ruled on a trustee's duty of undivided loyalty to the beneficiaries. *See, e.g.*, *Davoue v. Fanning*, 2 Johns. Ch. 252, 1 N.Y. Ch. Ann. 365 (Chancery Ct. of N.Y. 1816) (discussing 18th-century case law on the rule that a trustee owes a duty of undivided loyalty to the trust beneficiaries in the context of self-dealing and setting aside the sale of trust assets when the trustee was interested in the sale).
6. 103 N.Y. 58, 73–74, 8 N.E. 355, 358 (1886).
7. 302 N.Y. 246, 254, 97 N.E.2d 888, 891 (1951).
8. *Id.* (citing *In re Durston*, 297 N.Y. 64, 71–72, 74 N.E.2d 310, 313 (1947); *Meinhard v. Salmon*, 249 N.Y. 458, 464 & 468, 164 N.E. 545, 546 & 548, 62 A.L.R. 1 (1928); *Carrier v. Carrier*, 226 N.Y. 114, 125–26, 123 N.E. 135, 138 (1919); *Munson v. Syracuse, Geneva & Corning R.R. Co.*, 103 N.Y. 58, 73–74, 8 N.E. 355, 358 (1886).
9. For examples of such cases, see note 8.
10. 249 N.Y. 458, 164 N.E. 545, 62 A.L.R. 1 (1928).
11. *Id.* at 464, 164 N.E. at 546 (emphasis added) (quoting *Wendt v. Fischer*, 243 N.Y. 439, 444, 145 N.E. 303, 304 (1926)).
12. 92 N.Y. 56 (1883).
13. *Id.* at 65.
14. *Id.* at 66. While beyond the scope of this article, there are three types of cases involving exoneration of a trustee for retention: Cases in which the testator exonerates his trustee from loss for retaining assets that the testator has invested in and directed his trustee to retain, *see, e.g.*, *In re Clark's Will*, 257 N.Y. 132, 177 N.E. 397, 77 A.L.R. 499 (1931) (exculpatory clause upheld), cases in which the loss is occasioned by the trustee's investment and the trustee acted within the scope of his authority to retain assets, but in poor judgment, *see, e.g.*, *In re Olmstead*, 52 A.D. 515 (1st Dep't), 66 N.Y.S. 212, *aff'd*, 164 N.Y. 571, 58 N.E. 1090 (1900) (exculpatory clause upheld) and cases where, although exculpated for loss from retention of assets, the trustee acted outside the scope of his authority and breached his fiduciary duty, *see, e.g.*, *In re Hubbell's Will*, 302 N.Y. 246, 97 N.E.2d 888, 47 A.L.R.2d 176 (1951) (exculpatory clause invalid). *See also Legislation*, at 94–95 & nn. 29–31.
15. *Id.* at 65–66.
16. *Id.* at 66. (citations omitted).
17. *See* note 1, *supra*.
18. *See, e.g.*, *O'Hayer v. de St. Aubin*, 30 A.D.2d 419, 426, 293 N.Y.S.2d 147, 151 (2d Dep't 1968); *In re Cowles' Will*, 22 A.D.2d 365, 378, 255 N.Y.S.2d 160, 173–74 (1st Dep't 1965), *aff'd*, 17 N.Y.2d 567, 215 N.E.2d 509, 268 N.Y.S.2d 327 (1966); *In re City Bank Farmers Trust Co.*, 270 A.D. 572, 576, 61 N.Y.S.2d 484, 487 (1st Dep't), *aff'd*, 296 N.Y. 662, 69 N.E.2d 818 (1946).
19. 30 A.D.2d 419, 293 N.Y.S.2d 147 (2d Dep't 1968).
20. *Id.* at 426, 293 N.Y.S.2d at 151 (quoting III Scott on Trusts § 222.3, p. 1777 (3d ed. 1967)). For additional secondary authority and commentary on this rule, see Restatement (Second) of Trusts § 222 (2) (2003) and G. Bogert, Law of Trusts and Trustees, Ch. 26, § 542 (Rev. 2d ed. 1993 & 2002 pocket part); compare Uniform Trust Code § 1008 & Comment (2000) (Section 1008 is substantially similar to Section 222 of the Restatement (Second), except that under the UTC a grantor may exculpate his or her trustee from liability for personally profiting from his actions on behalf of the trust, so long as such profiting is not the result of bad faith or reckless indifference to the purposes of the trust or interests of the beneficiaries.).
21. 30 A.D.2d at 429, 293 N.Y.S.2d at 157 (Appendix).
22. *Id.* at 421, 293 N.Y.S.2d at 149.
23. *Id.* at 429–30, 293 N.Y.S.2d at 157–58.
24. *Id.* at 421, 293 N.Y.2d at 149.
25. 249 N.Y. 458, 164 N.E. 545 (1928).
26. 52 N.Y. 312 (1873).
27. 103 N.Y. 58, 8 N.E. 355 (1886).
28. 30 A.D.2d at 423, 293 N.Y.S.2d at 151 (emphasis added) (citing II Scott on Trusts § 170.09, p. 1321 (3d ed. 1967) and one case each from the New Jersey and Pennsylvania Supreme Courts).
29. *Id.* (citing *In re Hammer*, 16 A.D.2d 111, 225 N.Y.S.2d 868 (1st Dep't 1962) (per curiam), *aff'd*, 12 N.Y.2d 893, 118 N.E.2d 266,

237 N.Y.S.2d 1001 (1963) (mem.), *In re Balfe*, 245 A.D. 22, 280 N.Y.S. 128 (2d Dep't 1935), and *Heyman v. Heyman*, 33 N.Y.S.2d 235 (Sup. Ct., N.Y. Co. 1942)).

30. The majority in *Balfe* held that a trustee was exculpated from his malfeasance because the decedent had authorized the trustee to act without regard to whether the trustee had a personal interest in the same securities or companies as the trust, thereby depriving his estate of the benefit of the doctrine that forbids a trustee from acting under a divided loyalty. 245 A.D. at 24–25, 280 N.Y.S. at 130–31. In a strongly worded dissent, however, Presiding Justice Lazansky and Justice Young found the same provisions could not exculpate the trustee of the testamentary trusts, and even if they did, the trustee failed to act in good faith. *Id.* at 26, 280 N.Y.S. at 132. Moreover, the 1935 holding in *Balfe* is clearly inconsistent with the provisions of EPTL 11-1.7, making such exoneration against public policy in testamentary trusts.

In *Hammer*, the grantor established an *inter vivos* trust with a bank as trustee. Thereafter, the grantor guaranteed a third party's debt to the bank. When the bank filed an action against the grantor's estate to recover on the guarantee, the executor objected, arguing that the bank was subject to a divided loyalty that barred its recovery against the estate. 16 A.D.2d at 112, 225 N.Y.S.2d at 869. The court held that the bank did not waive the enforcement provision of the guarantee by agreeing to be trustee. *Id.* at 113, 225 N.Y.S.2d at 870. Therefore, *Hammer* does not stand directly for the proposition that a grantor may relax a trustee's duty of undivided loyalty to the trust. Moreover, two justices on the Appellate Division panel dissented in an opinion by Justice Bergan and would have held that the trustee owed an obligation of loyalty to the trust first and to its interest in collecting on its loan second. *Id.* at 113–14, 225 N.Y.S.2d at 870–71 (Bergan, J., dissenting). The principle that a trustee with competing fiduciary duties owes his duty to the trust first is actually well established under the laws of New York State. *See, e.g., In re Pulitzer*, 139 Misc. 575, 249 N.Y.S. 87 (Surr. Ct., N.Y. Co. 1931), *aff'd*, 237 A.D. 808, 260 N.Y.S. 975 (1st Dep't 1932).

Heyman involved an *inter vivos* trust established by a mother and father for their son's benefit. In pertinent part, the trust provided that the trustee "shall have the widest possible powers of investment embracing the right to enter into speculative transactions." 33 N.Y.S.2d at 240. The court held that although "this clause eliminates most if not all of the legal restrictions which, in the absence of the inclusion of such a specific provision, would safeguard and restrict trust investments, it clearly does not authorize the trustees to use the trust assets for their own benefit, to act in bad faith or recklessly to waste them." *Id.* While additional exculpatory provisions permitted the trustee to deal with and in assets in which both he, individually, and the trust held an interest, those provisions made specific reference to requiring the trustee to act in good faith. *Id.* at 240–41. Moreover, "in the absence of an express provision requiring a trustee to act in good faith," the law of New York would "impress such a trust character" upon the trustee." *Id.* at 241. Thus, *Heyman* stands for another proposition altogether that, despite "sweeping" exculpatory provisions, a grantor may not exculpate a trustee of an *inter vivos* trust from acting in good faith, regardless of whether good faith is explicitly stated in the trust or not. *Id.* at 242.

31. Moreover, it seems unlikely that the Court of Appeals would embrace a rule by which a trustee would be exculpated from liability by a mere inference of the grantor's intent, given the rule set forth in III Scott on Trusts § 222.4, p. 1778–79 (3d ed. 1967), that an exculpatory provision "is not effective to relieve the trustee of liability if it was inserted in the trust instrument by the person named as trustee and if in insert-

ing it he was guilty of an abuse of a fiduciary or confidential relations to the settlor." *Id.* at 1778; *see Jothann v. Irving Trust Co.*, 151 Misc. 107, 270 N.Y.S. 721 (Sup. Ct., N.Y. Co. 1934), *aff'd*, 243 A.D. 691, 277 N.Y.S. 955 (1st Dep't 1935); *see also* Restatement (Second) of Trusts § 222 (Comment) (providing factors to be considered); UTC § 1008(b) (creating a rebuttable presumption that an exculpatory clause drafted by a trustee is invalid). The Appellate Division in *O'Hayer* cited Section 222.3 of Scott on Trusts to support the enforcement of the exculpatory clause, but evidently apparently did not consider Section 222.4, perhaps because the trustees in *O'Hayer* were the grantor and his son. *See* note 20, *supra*.

32. *Id.* (citing *Industrial & Gen'l Trust, Ltd. v. Tod*, 180 N.Y. 215, 225–26, 73 N.E. 7, 9 (1905) ("No covenant of immunity can be drawn that will protect a person who acts in bad faith, because such a stipulation is against public policy, and the courts will not enforce it. The law requires the exercise of good faith, and no matter how strong the provision to shield from liability may be, there is no protection unless good faith is observed.") and *Balfe*, 245 A.D. 22, 280 N.Y.S. 128 (2d Dep't 1935)).
33. *Id.*; *see, e.g., New York State Med. Care Facilities Fin. Agency v. Bank of Tokyo Trust Co.*, N.Y.L.J., Dec. 20, 1994, p. 26, col. 4 (Sup. Ct., N.Y. Co.); *In re Akin*, N.Y.L.J., Oct. 23, 1989, p. 29, cols. 4–5 (Surr. Ct., Westchester Co.) (a trustee may be insulated from liability only so far as the specific exemption provided in an exculpatory provision); *see also* III Scott on Trusts § 222.2, p. 388–89 (4th ed. 1988); Restatement (Second) of Trusts § 174, Comment d (2003).
34. *See, e.g., In re Mallon's Estate*, 43 Misc. 569, 4 Mills 323, 89 N.Y.S. 554 (Surr. Ct., Kings Co. 1904), *aff'd*, 110 A.D. 61, 97 N.Y.S. 23 (2d Dep't 1905), *aff'd without opinion, sub nom. In re Howard*, 185 N.Y. 539, 77 N.E. 1189 (1906)).
35. 110 A.D. at 62–63, 97 N.Y.S. at 24.
36. *Id.* at 63–64, 97 N.Y.S. at 24 (citing *Crabb*, 92 N.Y. at 65, for the proposition that a fiduciary has committed "willful default" of his duties if he has "intentionally disregarded the rules which control and regulate the action of prudent and careful men in conducting their own business affairs."). For a comprehensive discussion of the meaning of the word "willful" in 1905, *see* the Appellate Division opinion in *Mallon* at 110 A.D. at 64–67, 97 N.Y.S. at 24–26.
37. 30 A.D.2d at 423 & 425–27, 293 N.Y.S.2d at 151 & 153–54.
38. *Id.* at 424–28, 293 N.Y.S.2d at 153–54.
39. N.Y.L.J., June 9, 1992, p. 23, col. 3 (Surr. Ct., N.Y. Co.) (citing *In re Mallon's Estate*, 110 A.D. 61, 97 N.Y.S. 23 (2d Dep't 1905)), *aff'd without opinion, sub nom. In re Howard*, 185 N.Y. 539, 77 N.E. 1189 (1906)).
40. *Id.*
41. *Id.* (citing *In re Rothko*, 43 N.Y.2d 305, 372 N.E.2d 291, 401 N.Y.S.2d 449 (1977) and *In re Ryan*, 291 N.Y. 376, 52 N.E. 909 (1943)).
42. *Id.*
43. *See also In re Daniel P. Scheuer*, N.Y.L.J., June 3, 1992, p. 23, col. 1 (Surr. Ct., N.Y. Co.) (essentially the same opinion as *In re Helen R. Scheuer* involving another of the forty Scheuer family trusts).
44. N.Y.L.J., June 18, 2002, p. 21, col. 4 (Surr. Ct., Nassau Co.).
45. *Id.*
46. *Id.*
47. *Id.* (citing *O'Hayer*).
48. *Id.* (citing *Bauer v. Bauernschmidt*, 187 A.D.2d 477, 589 N.Y.S.2d 582 (2d Dep't 1992)); *accord, In re Rice's Will*, 75

- N.Y.S.2d 578 (N.Y. Sup. Ct. 1940) (Schmuck, J.) In *Rice*, while providing little reasoning and citing no cases, Justice Schmuck held that clear language in the *inter vivos* trust “must be heeded unless . . . it is . . . against public policy.” Thus, according to the court, because Decedent Estate Law Section 125 had no application to the *inter vivos* trust, the court held that “no remainderman is authorized to object to the acts of the trustee during the lifetime of the grantor-life income beneficiary and that the objections of the guardian ad litem filed on behalf of the infant remaindermen be stricken out.” 75 N.Y.S.2d at 580.
49. 187 A.D.2d 477, 589 N.Y.S.2d 582 (2d Dep’t 1992).
 50. *Id.* at 478, 589 N.Y.S.2d at 583.
 51. *Id.* at 478–79, 589 N.Y.S.2d at 583 (citing cases).
 52. *See id.* at 477–79, 589 N.Y.S.2d at 583.
 53. *Id.* at 479, 589 N.Y.S.2d at 583.
 54. N.Y.L.J., July 24, 1998, p. 25, col. 3 (Surr. Ct., Kings Co.).
 55. *Id.* at p. 26, cols. 4-5.
 56. *Id.* at col. 5
 57. 162 Misc. 2d 888, 618 N.Y.S.2d 959 (Surr. Ct., Nassau Co. 1994).
 58. *Id.* at 893, 618 N.Y.S.2d at 963.
 59. *Id.*
 60. N.Y.L.J., Jan. 12, 1998, p. 32, col. 3 (Surr. Ct., Westchester Co.).
 61. *Id.* (emphasis added). The Surrogate also cited to *In re McAllister*, 144 Misc. 2d 994 (Surr. Ct., Nassau Co. 1989) a case involving a *testamentary* trust, in which Surrogate Radigan held that trust provisions that purported to exculpate a trustee from liability for retention and negligence were void under EPTL 11-1.7 and EPTL 11-2.1.
 62. 124 Misc. 2d 630, 476 N.Y.S.2d 763 (Surr. Ct., Nassau Co. 1984).
 63. 736 N.Y.S.2d 151 (3d Dep’t 2002).
 64. *See Carey v. Cunningham*, 191 A.D.2d 336, 336, 595 N.Y.S.2d 185, 185 (1st Dep’t 1993) (citing *O’Hayer* and *Balfe*) (affirming a Supreme Court New York Co. decision).
 65. Peter Valente & Joann T. Palumbo, *Exculpatory Provisions*, N.Y.L.J., Apr. 29, 1998, p. 3, col. 1.
 66. *Meinhard*, 249 N.Y. at 464, 164 N.E. at 546 (quoting *Wendt*, 243 N.Y. at 444, 145 N.E. at 304).
 67. A definitive rule from the Court of Appeals, while as equally welcome as a statute, seems unlikely given the extraordinary expense in bringing a case to the Court and the myriad of fact patters that can make any one case distinguishable from another.

**Ian W. MacLean is a trusts and estates attorney
in New York.**

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