

Avoiding Fiduciary Conflicts of Interest

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Avoiding Fiduciary Conflicts of Interest

Written by Carol Warnick – 7/16/18

It is very difficult for a trustee to have conflicts of interest without breaching the duty of loyalty. We typically think of trustee conflicts as they relate to self-dealing by the trustee, which is almost always a problem and for which the beneficiaries can obtain redress. But I have seen more conflicts lately in my practice where a trustee is trustee of different trusts that have conflicting interests, or the trustee is serving as trustee of a trust and also as personal representative of an estate whose interests are in direct conflict with each other.

When faced with a conflict situation, a trustee needs to take action before he or she breaches the duty of loyalty, which is a bedrock duty owed by all fiduciaries. *Restatement of Trusts § 78 (1)* states that a “trustee has a duty to administer the trust solely in the interest of the beneficiaries” That is not possible when the two trusts (or the trust and the estate) have conflicting interests and what the fiduciary does as trustee of one trust would be detrimental to the other. One

example would be engaging in a specific transaction that is beneficial to the beneficiaries of one trust but harmful to the beneficiaries of the other trust or of the estate.

Depending on the circumstances, a trustee could file a petition for instructions with the court, could obtain written consent from all the beneficiaries to engage in a certain transaction, or appoint an independent special trustee to serve solely for the purposes of engaging in the specific transaction. The *Restatement of Trusts § 78 comment c (1)* even discusses a “trustee ad litem.” It goes on to explain that a trustee ad litem would be appointed by the court without removing or displacing the trustee and would consider and handle a specific controversy or transaction where the trustee has a conflict. Not all of these suggestions are interchangeable — much will depend upon the language of the trust documents and the circumstances involved.

In fact, *Restatement of Trusts § 78 comment c (1)* also sets forth that a trustee may occupy conflicting positions where the trust instrument(s) contemplates or sanctions the conflict of interest. In short, the settlor of a trust can waive the rule of undivided loyalty by expressly providing for it in the trust document or

documents. However, even if approval of the conflict is given by the settlor in the document, the trustee still has a duty to act in good faith.

The key to avoiding problems is for the trustee to be sensitized to the issue of conflicts of interest and to take steps immediately when a conflict arises. Too many times I have seen trustees simply ignore the conflicts — at least until a beneficiary complains or brings a lawsuit — and by then the ability to take remedial action has long since passed.

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