Mediation and Arbitration have their limitations when it comes to trust disputes.

Unless the fiduciary issues and the representation issues in a trust dispute are properly sorted out in advance, there is a very real risk that an ill-considered rush to mediate or arbitrate will prove an expensive and time-consuming diversion to nowhere, or worse, exacerbate tensions while resolving nothing. The topic of mediating and arbitrating trust disputes is covered in pages 1209-1212 of *Loring and Rounds: A Trustee's Handbook (2012)*.

§8.44 Mediation and Arbitration Have Their Limitations When It Comes to Trust Disputes [*Excerpted from Loring and Rounds: A Trustee's Handbook (2012), pages 1209-1212*]

> *In drawing attention to the benefits of mediation, it would be simplistic to suggest it is a cure-all for all trust and probate disputes. Some disputes will not be appropriate for mediation, in particular those that turn on technical construction of trust deeds or wills, cases in which injunctions are sought and claims involving allegations of fraud*.[1]

Certainly no harm can come from endeavoring to mediate or arbitrate a contract dispute, particularly if all parties are of full age and legal capacity. A trust, however, is not a contract,[2] and, except in the case of a trust that is an instrument of commerce, *e.g.,* a mutual fund,[3] it is generally not incident to one. A trust is a fiduciary relationship with respect to property, in which the trustee generally will have numerous duties that run to the beneficiaries,[4] but in which the beneficiaries will have few if any duties that run to the trustee.[5] The parties to a contract, on the other hand, generally are not in a fiduciary relationship,[6] unless the same parties happen

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[1]Jeremy Gordon, *More talk*, 15(7) STEP J. 29 (July/Aug. 2007) (a publication of The Society of Trust and Estate Practitioners (STEP)).

[2]*See* Schoneberger v. Oelze, 208 Ariz. 591,595, 96 P.3d 1078, 1082 (2004) ("…[D]efendants face a fundamental problem that defeats their demand for arbitration…[, namely that] …the trusts at issue here…[are]…not contracts"). *See generally*§9.9.1 of this handbook (life insurance and third party beneficiary contracts generally).

[3]*See generally* Charles E. Rounds, Jr. & Andreas Dehio, *Publicly-Traded Open End Mutual Funds in Common Law and Civil Law Jurisdictions: A Comparison of Legal Structures*, 3 N.Y.U.J.L. & Bus. 473 (2007).

[4]*See generally*Chapter 1 of this handbook (defining the trust).

[5]*See generally*§5.6 of this handbook (duties and liabilities of the beneficiary).

[6]*See* Schoneberger v. Oelze, 208 Ariz. 591,595, 96 P.3d 1078, 1082 (2004) ("…[A] fiduciary relationship exists between a trustee and a trust beneficiary while no such relationship generally exists between parties to a contract").

simultaneously also to be in an agency or trust relationship.[7]

Moreover, many trusts bestow equitable property rights on unborn or unascertained individuals, or on individuals under some legal disability, *e.g.,* minority. Thus, unless the fiduciary issues and the representation issues are properly sorted out before hand, there is the very real risk that an ill-considered rush to mediate or arbitrate, at best, will be an expensive and time-consuming diversion to nowhere, and, at worst, will actually exacerbate the situation:

> One area that can cause serious complications in negotiation and drafting of nonjudicial agreements is failing to identify all of the parties interested in the matter. There are any number of individuals or entities who may have an interest in a matter and each interested party must be properly identified and given an opportunity to be heard. The failure to properly identify all of the parties interested in a matter can result in a nonjudicial agreement being deemed ineffective or a court determining that it does not have jurisdiction or that venue is improper in a judicial proceeding. In addition, the practitioner must make sure that in situations where a conflict exists or may exist, a virtual representative or special representative (or in the event of court proceedings, a guardian ad litem) is appointed to represent the interest of minor, incapacitated, unborn, or unascertained beneficiaries.[8]

Again, for a mediation or arbitration to bear fruit, all interested parties need to be a part of the process.[9] In the case of the typical trust dispute, that will generally mean that someone is going to have to go into court and seek to have it appoint a disinterested guardian ad litem who can represent the interests of the unborn and unascertained beneficiaries who are not virtually represented.[10] Otherwise, any agreement that is ultimately forged among the other parties will not be binding on the unborn and unascertained, at least to the extent that their equitable property rights may have been adversely affected.[11] Once the matter of a guardian ad litem is in the hands of the court, the dispute, like it or not, is for all intents and purposes in formal litigation, and the court may well have its own views on whether and how to mediate or arbitrate. Moreover, it is not unusual for a knowledgeable guardian ad litem, once appointed, to settle into the role of a quasi-mediator. If that happens, any plans for formal mediation or arbitration should probably be put on hold until such time, if ever, as it becomes clear that the involvement of the guardian at litem is either failing to break the logjam or actually exacerbating it.

A nonjudicial mediation or arbitration of a *breach-of-fiduciary-duty trust dispute* of which the actions of an incumbent trustee are the focus is at best awkward and at worst problematic and

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[7]*See generally* Charles E. Rounds, Jr., *Lawyer Codes Are Just About Licensure, the Lawyer's Relationship with the State: Recalling the Common Law Agency, Contract, Tort, Trust and Property Principles that Regulate the Lawyer-Client Fiduciary Relationship*, 60 Baylor L. Rev. 771 (2008).

[8]Gail E. Mautner & Heidi L. G. Orr, *A Brave New World: Nonjudicial Dispute Resolution Procedures Under the Uniform Trust Code and Washington's and Idaho's Trust and Estate Dispute Resolution Acts*, 35 ACTEC Journal 159, 180 (2009).

[9]*See generally*§5.7 of this handbook (the necessary parties to a suit brought by a beneficiary).

[10]*See, e.g.*, Mass. Gen. Laws ch. 190B, §§1-401, 3-1101, & 3-1102 (judicial approval of arbitrations and compromises involving Massachusetts trusts); Mark S. Poker & Amy S. Kiiskila, Prevention and Resolution of Trust and Estate Controversies, 33 ACTEC 262, 266 (2008). *See generally*§8.14 of this handbook (when a guardian ad litem (or special representative) is needed; virtual representation issues).

[11]*See, e.g.*, Mass. Gen. Laws ch. 190B, §3-1102.

costly.[12] The trustee continues to have an affirmative duty to act solely in the interest of the beneficiaries in matters pertaining to the trust.[13] Thus, any agreement that is the product of a mediation or arbitration between the trustee and the beneficiaries is not binding on a beneficiary who does not subjectively understand the applicable law and facts, unless, perhaps, if the beneficiary is being represented by independent counsel.[14] This is particularly the case when the duty of loyalty is implicated.[15] The principle applies even in the case of a beneficiary who is of full age and legal capacity. Moreover any nonjudicial resolution of a breach-of-fiduciary-duty trust dispute must be fair to the beneficiaries and reasonable: "A transaction between the fiduciary and the beneficiary in which the fiduciary is dealing on his own account in regard to a matter within the scope of the relation can be set aside if the transaction is not fair and reasonable. Thus, if a trustee purchases for himself property with the consent of the beneficiary, the beneficiary can set aside the sale if the price paid by the trustee was not in fact an adequate price, even though at the time of the sale the parties believed that it was adequate."[16]

Certainly the chances of having an agreement that is forged in a nonjudicial mediation or arbitration "stick" are enhanced if the trustee who is the subject of the dispute resigns before the nonjudicial process commences, if the successor trustee becomes a party to the mediation or arbitration, and if all parties are represented by independent counsel.[17] The problem is that if all that occurs, then the professional mediator or arbitrator risks becoming an expensive fifth wheel, and will certainly be one, in any case, if he or she is not at least as well versed in trust law as are

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[12]*See* Michael Heise, "*Why ADR Programs Aren't More Appealing: An Empirical Perspective*," paper presentation, Research Symposium on Empirical Studies of Civil Liability, Northwestern University School of Law, Chicago, IL (Oct. 9, 2008) (Abstract: "Standard law and economic theory suggests that litigating parties seeking to maximize welfare will participate in alternative dispute resolution (ADR) programs if they generate a surplus. ADR programs claim to generate social surplus partly through promoting settlements and reducing case disposition time. Although most associate ADR programs with trial courts, a relatively recent trend involves appellate courts' use of ADR programs. The emergence of court-annexed ADR programs raises a question. Specifically, if ADR programs achieve their goals of promoting settlements and reducing disposition time, why do some courts find it necessary to impose ADR participation? Attention to ADR's ability to achieve its goals provides one clue. Most empirical assessments of ADR programs' efficacy have been mixed. This study exploits a uniquely comprehensive database of state civil court trials and appeals and tests hypotheses germane to questions about whether court-annexed appellate ADR programs stimulate settlement and reduce disposition time. Using data from 46 large counties consisting of 8,038 trials that generated 965 filed appeals, with 166 appeals participating in ADR programs, findings from this study provide mixed support for ADR programs. Specifically, results from this study indicate that participation in an ADR program correlates with an increased likelihood of settlement but not reduced disposition time. ADR programs' mixed efficacy diminishes its appeal to litigants. Institutional interests help explain why appellate courts impose ADR participation notwithstanding mixed results on ADR efficacy.")

[13]*See generally*§6.1.3 of this handbook (duty of loyalty).

[14]*See generally*§7.2.7 of this handbook (informed consent).

[15]*See generally*§7.1.1 of this handbook (defenses to allegations that the trustee breached the duty of loyalty); Restatement of Restitution §191 (acquisition by a fiduciary/effect of consent of beneficiary).

[16]Restatement of Restitution §191, cmt. e.

[17]*See generally*§7.1.3 of this handbook (defense of consent, release, or ratification by the beneficiary).

the mediation or arbitration participants.[18] When it comes to trust disputes, retaining the services of an experienced and impartial trust lawyer to assist the parties collectively in framing the issues and ferreting out the applicable law is likely to be more efficient and cost-effective in the long run than going the formal mediation or arbitration route.

In any case, particularly if there is a guardian ad litem in the picture, the court has the last word, as no mediated settlement—and certainly no settlement that is inequitable—can relieve the court of its inherent and overarching equitable authority to supervise the administration of trusts.[19] The court is an agent neither of the fiduciaries nor of the beneficiaries. Not even a trust term that purports to oust the court of its traditional equitable jurisdiction over trust matters is enforceable, *e.g.,* one that purports to bestow on a member of the executive branch of a state's government the authority to make binding determinations as to whether the trustee is complying with the other trust terms.[20] Nor can the court be "ousted" by an expansive grant of discretion to the trustee. "It is submitted…that, even as to matters thus firmly committed to the trustee's discretion, judicial review should remain available if the trustee acts in bad faith, contrary to the terms of the trust, or with an improper motive."[21]

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[18]*See generally*§8.25 of this handbook (few American law schools still require Trusts).

[19]*See, e.g*., Mass. Gen. Laws ch. 190B, §3-1102(3) (providing that if the court finds a particular contest or controversy "is in good faith and that the effect of the agreement upon the interests of persons represented by fiduciaries or other representatives is just and reasonable, shall make an order approving the agreement and directing all fiduciaries subject to its jurisdiction to execute the agreement"). *Cf*. Mark S. Poker & Amy S. Kiiskila, *Prevention and Resolution of Trust and Estate Controversies*, 33 ACTEC 262, 266 (2008) ("If a dispute involves trust beneficiaries, however, it is not clear whether an arbitration provision can require the beneficiaries to participate or relinquish their rights to litigate in the court system").

[20]*See generally* 3 Scott & Ascher §18.2 (Executive Branch Encroachment on Court's Equitable Prerogatives). *Cf*. §9.4.4 of this handbook (legislative branch encroachment on court's equitable prerogatives).

[21]3 Scott & Ascher §18.2 (Control of Discretionary Powers).