

A Future Full of Trust Contests

by Curtis E. Shirley

The following article focuses on the typical situation where the Settlor signs a revocable Trust. Although the ultimate expenses and taxes are similar, there are many reasons clients choose a Trust over a Will. The same Trustee can keep investment authority over the Settlor's property for decades after death. This reason alone has the insurance industry, investment brokers and financial planning companies recommending them. If the decedent signed a poorly written Will, hell has to freeze over for a Court to change it. But Courts can reform, rescind or even terminate a Trust for just about any reason that sounds good, such as correcting a mistake by the drafting attorney, or a change in circumstances. Wills cannot threaten to disinherit a contesting heir, or condition inheritance in restraint of a future marriage. Who knows about Trusts, but drafters might as well try. Because terms of a Trust supercede sections of the Indiana Code unless they violate a "clear prohibition", in terrorem clauses and restraints of marriage are the tip of the iceberg of how a Settlor might control his or her property well into the future.

Trusts are also easier to prepare and sign. It needs no formal language; any writing qualifies if it sufficiently describes the Trust property and a beneficiary's interest. Although an attorney in fact cannot sign another's Will, which takes two witnesses, there are no such niceties in signing and funding a Trust. Its terms can even provide for modifications by someone other than the Settlor.

Avoiding probate has advantages. Executors must pay for bonds and notices in the newspaper. Trustees need not. Executors cannot be a convicted felon - Trustees can administer property from their jail cell. Executors collect assets and file an inventory - Trustees get involved when they want and file accountings only with income beneficiaries once a year. A more secretive affair. Executors better get written permission from all heirs or Court authority to sell any property. Trustees have the freedom to sell or distribute property immediately to beneficiaries. Even after most estate matters are concluded it usually takes an extra month for the Court to examine the final accounting and give heirs an opportunity to object at a hearing. Silly waste of time.

But probate has its advantages. Creditors have only five months after the first published notice to file a claim. Creditors of a Trust should be able to use the two to twenty year limitations

periods. If an Executor waits more than five months to open an estate, the decedent's real estate is protected from creditors. Any real estate in a Trust is considered personal property so it is never immune. Executors are released from liability with Court approval of a final accounting. Even complaints based upon fraud are extinguished after a year. Trustees have at least two years of liability after a beneficiary has reason to know of the Trustee's conversion, mistake or fraud. Considering how many beneficiaries are unborn or minors, limitation periods against Trustees might never end.

What is amazing is that the Indiana legislature has provided technical and precise procedures to effectuate a Last Will & Testament. Detailed rules apply to construing Wills, contesting them, and even reviving them. But not so with Trust matters. Unless Trust terms specifically provide, after born children, illegitimate children, pretermitted heirs, and adopted children fair far better under a Will than a Trust. The Probate Code makes allowance for advancements to heirs, and disinherits a spouse living elsewhere in adultery or that abandons the other without cause. The Trust Code could care less.

Plaintiffs file Will contests usually when he or she has a greater slice of the pie in a prior Will. The doctrine of dependent relative revocation looms large. Indiana Code Section 29-1-5-6 states that a prior Will is revived if "it shall appear by the terms of such revocation to have been his intent to revive it." The cases have used this as a platform to hold that a testator is presumed to have revoked a prior Will by signing a subsequent Will only if that subsequent Will proves effective. See Roberts v. Fisher, 105 N.E.2d 595 (Ind. 1952); Flagle v. Martinelli, 360 N.E.2d 1269 (Ind.App. 1977). This rule operates pretty smoothly unless the testator tore up a prior Will and got around to signing a subsequent Will much later.

But what about dependent relative revocation for a Trust? The simple case would be a plaintiff that contests a Trust Amendment, and if successful the amendment is ignored and the Trust terms control. The more difficult case is where the Trust is fully funded, then revoked, and the property transferred to a subsequent Trustee. Because a Will is ambulatory (in that it takes effect only upon a person's death), and a Trust takes effect when signed, I doubt that the Courts can fashion any definitive rules concerning dependent relative revocation in Trust contests. Yet this issue goes to the very heart of filing it in the first place. If the plaintiff asks the Court to throw out a Trust, the property Will probably go into the Estate (and

not into a prior Trust). And if the Will pours into a defective Trust, everything may go by intestacy.

For Will contests the Probate Code specifically sets out the allegations of the complaint, the parties, requirements of notice, bond, burdens of proof, and the limitations period within which plaintiffs must file. It even provides for attorney fees. Although the Trust Code mentions none of these, this article attempts to address the major ones.

Filing the Trust Contest

What should the complaint allege? In a typical Will contest, he or she alleges simply the following:

- (1) the unsoundness of mind of the testator;
- (2) the undue execution of the Will;
- (3) that the Will was executed under duress or was obtained by fraud;
- (4) any other valid objection to the Will's validity or the probate of a Will.

In a Trust contest, in the writer's experience, no complaint has been dismissed where the plaintiff makes similar allegations. It remains to be seen whether the same standard for setting aside a Will also applies to setting aside a Trust.

Of the allegations that set aside a Will, issues of undue influence, duress and fraud should be the same no matter what document we're talking about. But most Will contests focus on the decedent's soundness of mind. The tougher question is whether Settlers need a sound mind to sign a Trust.

Indiana Code Section 30-4-2-10(b) provides that "if the Trust is created by a transfer of property in Trust, the transferor must have the same capacity as if he had made a non-Trust transfer of the property." This seems to mean that to create a Trust involves the same standard as making a gift. This standard applies whether the Settlor transfers the property in Trust to himself as Trustee or to another. But if the Settlor transfers the property to himself as Trustee (and not another), Indiana Code Section 30-4-2-11(a) provides an additional standard for capacity to receive the property: "If the Trustee is a natural person, he must have the capacity to take, hold, and deal with property for his own benefit and must be at least

eighteen (18) years of age, be of sound mind and good moral character.” (Emphasis added).

In Bowden v. Elston Bank & Trust Co. of Crawfordsville, 117 Ind. App. 612, 75 N.E.2d 170 (1947), the court did not define Trust capacity but indicated that the evidence showed that the Settlor was of sound mind at the time of executing the Trust because she was fully aware of what she was doing and knew her property, heirs, why she did not want them to have property, whom she wanted to have it and why.

To make a valid inter vivos gift in Indiana requires one to have the mental capacity to understand what she is doing, the extent and value of her property, the ability to recollect the property she is disposing of, the persons who are the natural objects of her bounty, and the manner in which she is distributing the property among them. Thorn v. Cosand, 67 N.E. 257 (Ind. 1903). In a more recent decision, Shourek v. Sterling, 652 N.E.2d 865 (Ind.App. 1995), the Court held that an inter vivos gift occurs when the donor is competent to contract, has freedom of Will, intends to make gift, the gift is completed with nothing left undone, property is delivered and accepted, and the gift is immediate and absolute.

The test for determining a person's mental capacity to contract is whether the person was able to understand in a reasonable manner the nature and effect of his act. "In order to avoid the contract, the person must not only have been of unsound mind, but also have had no reasonable understanding of the contract's terms due to his instability." Gallagher v. Central Indiana Bank, N.A., 448 N.E.2d 304 (Ind.App. 1983); See Dougherty v. Dougherty, 115 Ind. App. 253, 57 N.E.2d 599 (1944).

Compare these standards to other jurisdictions. At the lowest end of the spectrum is testamentary capacity. Florida, Arkansas, and Maryland take this approach. Rose v. Dunn, 679 S.W.2d 180 (Ark. 1984); Boyle v. Rody, 180 Md. 471, 25 A.2d 457 (Md.App. 1942). At the highest end of the spectrum requires a Settlor to have the capacity to sign a contract. Illinois and New York take this approach. Matter of ACN, 133 Misc.2d 1043, 509 N.Y.2d 966 (Supr.Ct. 1986); Ortelere v. Teacher's Retirement Board, 25 N.Y.2d 196, 303 N.Y.2d 362 (1969).

If Indiana follows the soundness of mind standard, then the law in Will contests Will thoroughly explain the issue. But if Shourek is expanded from the gift context to Trusts, Illinois law provides a more thorough treatment. See Jackson v. Pillsbury, 380

Ill. 554, 573, 44 N.E.2d 537, 546 (1942). A Settlor can create a Trust only where he has the legal competence to dispose of the legal title to his property. 76 Am.Jur.2d, Trusts, Section 55, p.84; Schumann-Heink v. Folsom, 328 Ill. 321, 159 N.E. 250 (Ill. 1927) ("He has the same power to create Trusts as he has to alienate the legal title to his property"). To revoke a Trust, the Settlor needs to have the mental capacity to understand the nature of the transaction, "not necessarily an aptitude in dealing with financial matters." 76 Am.Jur.2d, Trusts, Section 99, p.136-37. The test of mental capacity is whether the grantor was capable of transacting ordinary business affairs. Ring v. Lawless, 190 Ill. 520, 532-33, 60 N.E. 881, 885 (1901). Transacting ordinary business is defined as the "Mental strength to compete with an antagonist and understanding to protect his own interest. ... The mental strength sufficient to fully comprehend the nature of his transaction, ... the value of what he was conveying and the liabilities he was assuming." Thatcher v. Kramer, 347 Ill. 601, 609, 180 N.E. 434, 437 (1932) (citing the Ring case) ("The mere fact that the grantor comprehended that he was making a deed is not in itself sufficient to sustain the transaction.").

In Oak Park Trust & Savings Bank v. Fisher, 225 N.E.2d 377 (Ill.App. 1967), the trial court invalidated a Trust revocation. The Court of Appeals affirmed, noting that the doctor testified that the Settlor was incompetent and "mentally incapable of having the care, custody and management of her property, affairs and estate and does not know her exact bounty and does not know the exact objects of her bounty." 225 N.E. at 378-79. The parties focused on the word "competency" without any further definition.

So where does this leave us? If you need only a sound mind to sign a Trust, the contesting plaintiff asks the following questions:

- (1) In your opinion was the decedent of unsound mind?
- (2) Did he have sufficient strength of mind and memory to enable him to know the extent and value of his property?
- (3) Did he know the number and names of those who were the objects of his bounty?
- (4) Did he know their deserts with reference to their conduct toward and treatment of him?
- (5) Did he have the ability to retain those facts in mind long enough to have his Will prepared and executed?

See Farner v. Farner, 480 N.E.2d 251 (Ind.App. 1985). If the plaintiff gets a "No" answer to any of the above questions (with

sufficient supportive facts), you're headed for trial. But until the Indiana appellate courts rule on this issue, questions in a deposition and standards used in summary judgment briefs and Jury instructions should focus on all of the other possibilities:

- (1) In your opinion did the decedent have the capacity to make a non-Trust transfer of his property?
- (2) Did he have the capacity to take, hold, and deal with property for his own benefit and be sound mind and good moral character?
- (3) Was he fully aware of what he was doing, knew his property, heirs, why he did not want them to have property, whom he wanted to have it and why?
- (4) Did he have the mental capacity to understand what he was doing, the extent and value of his property, the ability to recollect the property he was disposing of, the persons who are the natural objects of his bounty, and the manner in which he is distributing the property among them?
- (5) Was he competent to contract, have freedom of Will, intending to make a gift, with nothing left undone, where the property was delivered and accepted, and the gift was immediate and absolute?
- (6) Was he able to understand in a reasonable manner the nature and effect of his act?
- (7) Did he have a reasonable understanding of the contract's terms despite his instability?
- (8) Did he have the legal competence to dispose of the legal title to his property?
- (9) Did he have the ability to alienate the legal title to his property?
- (10) Did he have the mental capacity to understand the nature of the transaction, not necessarily an aptitude in dealing with financial matters?
- (11) Was he capable of transacting ordinary business affairs?
- (12) Did he have the mental strength to compete with an antagonist and protect his own interest?
- (13) Did he have the mental strength sufficient to fully comprehend the nature of his transaction, the value of what he was conveying and the liabilities he was assuming?
- (14) Was he mentally capable of having the care, custody and management of his property, affairs and estate and

know his exact bounty and the exact objects of his bounty?

Attorneys filing Trust contests swim in shark filled waters. And with so many unknowns, these cases can last a very long time.

When should a plaintiff file?

If a Will contest is not filed within five (5) months of the admission of the decedent's Will to probate, the beneficiaries can breath a sigh of relief. Not so with a possible Trust contest. Indiana Code Section 34-1-2 et al. states that the limitations period may be as low as two (2) years (for allegations concerning personalty), or as high as six (6) years (for allegations concerning actual or constructive fraud). See Malikowski v. Banc One, 590 N.E.2d 559 (Ind. 1992); Tenta v. Guraly, 221 N.E.2d 577 (Ind.App. 1966). Thus, while an estate beneficiary has legitimate expectations of keeping an inheritance approved by the Court, a Trust beneficiary cannot enjoy similar protections until much more time has passed.

Once the theory of liability determines which limitations period applies, the next problem is when did the limitations period begin? In a Will contest the five month period begins on the date the Court admitted the Will to probate. For a Trust contest, the date of the decedent's death and any Court order concerning probate matter little. I suspect that the Courts will apply the discovery rule, finding that the limitations period begins to run when the plaintiff knew, or in the exercise of ordinary diligence could have known, that he or she sustained an injury. See Habig v. Bruning, 613 N.E.2d 61 (Ind.App. 1993), relying on Wehling v. Citizens Nat. Bank, 586 N.E.2d 840 (Ind. 1992). The usual arguments concerning laches, waiver, estoppel, and tolling should also apply. In the writer's opinion, for all revocable Trust cases the limitations period Will begin no earlier that the Settlor's death because there is no injury prior to that time. As a practical matter the accrual date could bee much later. I cannot see how any limitations period can begin until the beneficiary has reason to know about a possible interest in the Trust.

Who are the parties?

In a Will contest the plaintiff must include the Executor as a defendant (and all beneficiaries listed in the Will). So it is wise for the Trust contest plaintiff to name the Trustee and all interested beneficiaries as well, although no statute requires this. As an evidentiary matter, the impact of the Deadman's Statutes on a Will

contest cannot be understated. They are based upon the principle that when the lips of one party are closed by death, the lips of other parties are closed by law. See IAG Henry, The Probate Law and Practice 158 (Grimes Ed. 1978). Take for example the typical situation where a claim is filed in the estate. Indiana Code Section 34-45-2-4 prevents the claimant from testifying because the executor is a party and the claimant is adverse to the Estate. The same cannot be said in the Trust context. Section 34-45-2-4 does not apply because the Executor is not a party (only the Trustee). How the Trustee can defend is a serious problem.

The other typical situation involving the Deadman's Statute is where the plaintiff files a Will contest. Indiana Code Section 34-45-2-5 applies to suits by or against "heirs or devisees founded on a contract with or demand against the ancestor." All of the them are barred from testifying "as to any matter that occurred before the death of the ancestor." If all parties to a Will contest are barred by this rule, all parties to a Trust contest should likewise be barred. See Lee v. Schroeder, 529 N.E.2d 349 (Ind.App. 1988); Bechert v. Lehe, 161 Ind.App. 454, 316 N.E.2d 394 (1974); Loeser v. Simpson, 219 Ind. 572, 39 N.E.2d 945 (1942). The only exception to this rule concerns testimony about the decedent's soundness of mind. The theory behind the exception is that matters pertaining to the decedent's mental state through his actions and statements are open to public view and not within the peculiar knowledge of the parties involved. See Lamb v. Lamb, 105 Ind. 456, 5 N.E. 171 (1886); Lee v. Schroeder, 529 N.E.2d 349 (Ind.App. 1988). There is every reason to assume that this exception would also apply to Trust contests.

What is the remedy?

In a Will contest there is no middle ground. It is either valid or not. In some limited cases of undue influence, there is some law that a naughty defendant can be stripped of his or her inheritance and the remainder of the Will stand. But with a Trust contest, the sky is the limit on the remedies an ingenious plaintiff might seek. As to the ordinary Trust contest the Court Will most likely declare it valid or void. As stated earlier, however, the Court has discretion to rescind, revoke, or even reform a Trust, which a Court lacks concerning a Will. The plaintiff may also seek a constructive Trust over the property, surcharge the Trustee, have the beneficiaries return the property, or seek damages from responsible defendants.

Do you get a Jury?

In most Trust contests the plaintiff or the defendant requests trial by Jury and the Courts permit it without question. What I would like to raise are the arguments that often go unnoticed that Trust litigation in general should not involve a Jury because the real issue is whether the Court should place a constructive Trust over the assets.

The right to a Jury trial is linked to the question of whether the case involves a matter of law or equity. Trial Rules 38 and 39 are the initial rules that apply. Trial Rule 39(A)(2) states that if a party demands trial by Jury on any issue upon which he is entitled to a Jury trial, the court should grant a Jury as to that issue. But subsequent case law has rejected this approach. A party is not entitled to a Jury where any essential part of the case is in equity. See Baker v. R & R Construction, Inc., 662 N.E.2d 661, 665-66 (Ind.App. 1996); Hiatt v. Yergin (1972), Ind.App., 284 N.E.2d 834; Sikich v. Springmann (1943), Ind., 48 N.E.2d 808, *cert. denied*, 320 U.S. 783. The Court looks to the pleadings "and their general scope and tenor. If an essential part of a cause of action is equitable the rest of the case is drawn into equity." Baker, 662 N.E.2d at 665 (no Jury was allowed where the Bank's foreclosure on a mechanic's lien and the defendants' later action for breach of fiduciary duty were consolidated).

Where the plaintiff chooses to attack a Trust, the suit attempts to rescind and cancel a written instrument, a matter entirely of equity. See Fish v. Prudential Insurance Company of America (1947), Ind., 75 N.E.2d 57. If the matter is labeled as one seeking a constructive Trust, see Matter of Estate of Neu (1992), Ind.App., 588 N.E.2d 567, the case is entirely equitable. See Givens v. Rose (1978), Ind.App., 383 N.E.2d 448. Even if the case raises issues of undue influence, unsoundness of mind or undue execution, the case would still be within the equitable jurisdiction of the Court. See Daugherty v. Daugherty (1947), Ind.App., 75 N.E.2d 427, 429.

There are numerous cases in which it has been held that where the title to land or chattels or money is obtained by undue influence exerted by the transferee upon the transferor, a constructive Trust arises. Thus where a person who is in a fiduciary or confidential relation to another obtains property from the other by taking advantage of the relation, a constructive Trust arises.

William F. Fratcher, SCOTT ON TRUSTS, v1.5, sec.468, pp.357-58 (4th ed. 1989) (and two pages of cases cited therein).

Simply put, whatever issues of fact arise in Trust litigation, the Court has equitable jurisdiction to decide the matter. See Daugherty, 75 N.E.2d 427 (where plaintiff sought to set aside a deed); Martin v. Martin (1889), Ind., 20 N.E. 763. See Hall v. Indiana Dep't of State Revenue (1976), Ind.App. 351 N.E.2d 35 (constructive Trust the proper remedy where client had deeded land to her attorney); Reiss v. Reiss (1986), 500 N.E.2d 1223 (constructive Trust the proper remedy where dispute concerns ownership of moneys removed from joint bank accounts); Rollins v. Metropolitan Life Ins. Co., 912 F.2d 911 (7th Cir. 1990) (applying Indiana law, a constructive Trust was the proper remedy concerning ownership of life insurance proceeds).

Whether the Complaint requests "damages" is not conclusive. In Midwest Fertilizer Co. v. AG-Chem Equipment (1987), Ind.App., 510 N.E.2d 232, "Indiana recognizes that the character of an action is determined by its substance, not its caption or formal denomination. In making such a determination, we must examine the totality of the pleadings and relief sought." Id. at 233 (citations omitted). In Martin v. Martin (1889), Ind., 20 N.E.2d 763 at 767, "The nature of the cause of action must be determined from the substantive facts therein pleaded, and not from the prayer for relief, nor from the name given to the action by the pleader."

Do you get attorney fees?

As to defendants, a Trustee has the duty to defend actions for the protection of Trust property and of himself in the performance of his duties. Indiana Code Section 30-4-3-3(a)(11) & 30-4-3-6(b)(10). As such, the Trust is entitled to defend complaints and incur reasonable attorney fees as an expense of Trust administration. Id. at 30-4-5-11(a)(4); Matter of Fitton, 605 N.E.2d 1164, 1174 (Ind.App. 1992); Gray v. Union Trust Co., 213 Ind. 675, 14 N.E.2d 532 (1938).

The amount of attorney fees does not depend upon the result of the litigation but on the reasonable necessity for such litigation. Other considerations include whether the Trustee is acting reasonably and in good faith, whether the issues have consequence to the estate or beneficiaries, whether the facts are disputed that would require a trial, whether the legal questions are simple or complex, settled by precedence or open to serious debate, and the necessity for litigation and multiple employment of attorneys. See Zaring v. Zaring, 39 N.E.2d 734, 737 (Ind. 1942).

As against the beneficiaries, attorney fees are recoverable by the Trustee against the beneficiary (or charged against the

beneficiary's ultimate share) where the Court specifically finds that the litigation was frivolous, unreasonable, groundless, or litigated in bad faith. Matter of Fitton, 605 N.E.2d 1164, 1173 (Ind.App. 1992) (and cases cited therein).

As to the plaintiffs, in a Will contest the attorneys get paid for winning and for losing (as long as you have a good faith case) pursuant to Indiana Code Section 29-1-10-14. In a Trust contest, however, no similar statute exists. If the plaintiffs are not successful, you have an outside chance of getting paid by arguing that you have provided a benefit to the Trust. But get your money up front.