

**Does an Exculpatory Clause Protect Trustees
Against Claims of Breach of Fiduciary Duty?**

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The starting point for evaluating whether trustees have breached a fiduciary duty is the settlor's intent as provided in a trust instrument, and many trusts contain clauses known as "exculpatory" clauses. These clauses often are designed to immunize trustees from liability to beneficiaries absent something beyond "ordinary" negligence. Years ago, such clauses were held unenforceable as against public policy, but the modern trend, which is captured by the Restatement and uniform statutes, allows for enforceability of these clauses with certain limitations. Common examples of exculpatory clauses that normally are enforced include clauses absolving the trustees of liability so long as they act in "good faith," and clauses that only provide for liability in situations of "gross negligence" or reckless or intentional conduct. However, courts will not enforce clauses providing trustees with blanket immunity for any actions.

Section 222 of the Restatement (Second) of Trusts, which is identical to the same section of the Restatement (First) of Trusts, provides:

- (1) Except as stated in Subsections (2) and (3), the trustee, by provisions in the terms of the trust, can be relieved of liability for breach of trust.
- (2) A provision in the trust instrument is not effective to relieve the trustee of liability for breach of trust committed in bad faith or intentionally or with reckless indifference to the interest of the beneficiary, or of liability for any profit which the trustee has derived from a breach of trust.
- (3) To the extent to which a provision relieving the trustee of liability for breaches of trust is inserted in the trust instrument as the result of an abuse by the trustee of a fiduciary or confidential relationship to the settlor, such provision is ineffective.

Restatement 2d Trusts § 222 (1959); see Restatement 1st Trusts § 222 (1935).

The Restatement (Third) of Trusts slightly expands upon the situations in which an exculpatory clause may be rendered ineffective, providing that such a clause will be ineffective if it attempts to protect trustees from a breach of trust made with indifference to the fiduciary duties of the trustees, the terms or purposes of the trust, or the interests of the beneficiaries:

- (1) A provision in the terms of a trust that relieves a trustee of liability for breach of trust, and that was not included in the instrument as a result of the trustee's abuse of a fiduciary or confidential relationship, is enforceable except

to the extent that it purports to relieve the trustee

(a) of liability for a breach of trust committed in bad faith or with indifference to the fiduciary duties of the trustee, the terms or purposes of the trust, or the interests of the beneficiaries, or

(b) of accountability for profits derived from a breach of trust.

Restatement 3d Trusts § 96(1) (2012).

The Restatement sections are similar, although not identical, to the relevant section of the Uniform Trust Code ("UTC"). Section 1008 of the UTC provides:

(a) A term of a trust relieving a trustee of liability for breach of trust is unenforceable to the extent that it:

(1) relieves the trustee of liability for breach of trust committed in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries; or

(2) was inserted as the result of an abuse by the trustee of a fiduciary or confidential relationship to the settlor.

(b) An exculpatory term drafted or caused to be drafted by the trustee is invalid as an abuse of a fiduciary or confidential relationship unless the trustee proves that the exculpatory term is fair under the circumstances and that its existence and contents were adequately communicated to the settlor.

UTC § 1008 (2000). While the UTC and Restatement sections address the insertion of the exculpatory clause into the trust instrument, the requirements of the UTC section in this regard are more onerous. Where the exculpatory clause is "drafted or caused to be drafted" by the trustees, the UTC places the burden on them to prove the clause is fair and its "existence and contents were adequately communicated to the settlor." UTC § 1008.

What is clear from both the UTC and Restatement sections is that the trustees cannot be immunized completely. Otherwise, no trust relationship would exist. "A trust implies an equitable duty to apply for the benefit of the beneficiary," and "[a]n immunity clause covering all possible breaches of trust connotes no enforceable duty at all toward the beneficiary, or else no remedy for breaches of duty which are unconscionable." G. Bogert & G. Bogert, *Law of Trusts and Trustees* § 542, p. 188-89 (rev. 2d ed. 1993).

Many states follow approaches comparable to the Restatement or UTC approaches, including Pennsylvania and New Jersey. *See, e.g.*, 20 Pa. Stat. § 7788 (adopting UTC § 1008); N.J. Stat. § 3B:31-77 (adopting UTC § 1008); *see also In re Niessen's Estate*, 413 A.2d 1050, 1053 (Pa. 1980) (citing Restatement 2d Trusts § 222 with approval); *Gouley v. Land Title Bank & Trust Co.*, 198 A. 7, 9 (Pa. 1938) (citing Restatement 1st Trusts § 222 with approval, and stating provisions "defining the duties of the trustee and exempting it from liability except for gross negligence or willful and intentional breach of trust are valid and enforceable"); *Farr v. 1st Camden Nat'l Bank & Trust Co.*, 66 A.2d 444, 446 (N.J. Super. Ct. 1949) (citing Restatement 1st Trusts § 222 with approval). In contrast, some states take a more restrictive approach and still consider exculpatory clauses to be against public policy in many situations—most notably, New York. *See, e.g.*, N.Y. Est. Powers & Trust Law § 11-1.7; *Estate of Lubin*, 539 N.Y.S.2d 695, 696-97 (N.Y. Sur. Ct. 1989) (finding clause purporting to relieve executor from liability "for any loss or injury to the property...except...as may result from fraud, misconduct or gross negligence" void as against public policy).

In states that do enforce exculpatory provisions, a frequent issue is whether the trustees' conduct in question falls within the scope of the provision, and typically exculpatory provisions are strictly construed. Given this and the historical scrutiny of exculpatory clauses, trustees in states following the Restatement or UTC approaches must be cognizant that, while they may obtain some benefit from exculpatory clauses, such clauses offer limited protection, at best. Under any circumstances, trustees must not act in bad faith or engage in intentional misconduct.