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## Report of Working Group on Representing Fiduciaries

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# REPORT OF WORKING GROUP ON REPRESENTING FIDUCIARIES\*

## INTRODUCTION

Following the general Conference plan, the working group first identified the broad range of ethical issues which could arise in the representation of fiduciaries. The group distinguished between the role of a lawyer who represents a fiduciary individually, such as in a matter unrelated to the fiduciary estate, or who advises the fiduciary in an action brought by beneficiaries alleging wrongdoing on the part of the fiduciary, and the role of a lawyer who represents a fiduciary serving in a fiduciary capacity. The group focused its discussion on the latter role with emphasis on the ethical dilemmas which arise when the lawyer becomes aware of actions by the fiduciary which negatively impact some or all of the beneficiaries.

### I. HYPOTHETICALS AND QUESTIONS RAISED

#### A. *Hypotheticals*

To assist in the discussion, participants focused on the following two hypotheticals developed by Professor Jeffrey Pennell:

##### 1. Hypothetical (1)

The administrator of an estate (A) hired Lawyer (L) to represent A and administer the pour over trust of decedent (D). The fiduciary is D's son from a prior marriage. D's estate plan provides for his surviving spouse (S) for life, remainder to his children from the prior marriage.

A controversy arises over how the estate should be managed. The son wants to invest the trust so that it will grow during S's lifetime. S, however, is concerned about paying for long-term care and wants the trust to generate maximum income.

It appears to L that S's capacity is diminishing. She has no counsel of her own. L learns that the children have secretly been using the trust funds to make loans to their business.

##### 2. Hypothetical (2)

Lawyer (L) represents a man (S) who is the guardian of the person and substantial property of his father, who has mental disabilities. The guardian is the father's sole heir.

L suspects that much of the father's confusion may be caused by the medications he takes, but the son refuses to have the medications adjusted. S, claiming they are unnecessary luxuries which squander the estate, refuses to pay for certain items for which the father expresses a desire. L learns that S has misappropriated estate funds and that he intends to conceal this in future accountings filed with the court.

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### B. *Questions Raised*

By asking and attempting to answer the following questions, participants sought to determine the parameters of representation of a fiduciary serving in a fiduciary capacity. These individuals may include a trustee, personal representative, an executor or administrator, or a guardian or conservator. The group asked:

1. Who is the client?
  - a. The fiduciary?
  - b. The beneficiary of the fiduciary entity?
  - c. The entity itself?
2. To whom does the lawyer owe a duty?
  - a. To the fiduciary who hired the lawyer?
  - b. To the beneficiary of the fiduciary entity?
  - c. To third parties, for example, creditors?
  - d. To the entity itself?
  - e. Is the duty in guardianships higher than that in estates or trusts?
  - f. What happens if there are multiple fiduciaries who disagree or if the interests of two or more beneficiaries are divided?
  - g. Can an attorney represent a fiduciary both as fiduciary and as an individual?
3. From what source does the duty derive?
  - a. Is the duty ancillary to, or does it derive from, the attorney-client relationship?
4. What obligations does the duty impose?
  - a. Can the lawyer disclose otherwise confidential information?
  - b. If so, to whom and under what circumstances?
  - c. Is the disclosure optional or mandatory?
5. How, and at what point, should the lawyer communicate the boundaries of his or her role to the client?
  - a. Should the lawyer communicate this role to the beneficiaries?
  - b. To third parties?
  - c. If so, by what means?

## II. DISCUSSION

Members of the working group disagreed with respect to both the extent of a lawyer's duties and the party to whom those duties are owed. All participants agreed, however, that consideration of these issues is fundamental to any review of the role of the lawyer and that any effort to resolve them must involve clarification of the Model Rules of Professional Conduct ("Model Rules"), development of practice guidelines, and education of the bar, the judiciary, and fiduciaries.

### A. *Existing Authority*

The group first discussed the existing authority in the field. Professor Pennell illustrates the ethical dilemmas most frequently encountered by

lawyers representing fiduciaries.<sup>1</sup> Professor Pennell poses a series of hypothetical situations for discussion and notes that court decisions and ethics opinions on these issues are limited, usually originating in the areas of legal malpractice, evidentiary privilege, and fee disputes. He analyzes existing treatises and opinions which have addressed the relationships more comprehensively. These reach widely varying conclusions regarding to whom the lawyer's duties should flow, from what source they derive, and the obligations they impose.

Noting the important distinction between the attorney-client relationship and the duties to non-clients which derive from that relationship, Professor Pennell cautions against imposing "untenable or undefinable" obligations on the lawyer. He does, however, recognize that the lawyer who represents a fiduciary owes more to other fiduciaries and to beneficiaries than might be the case in different matters. Pennell concludes that, in order to "do the right thing" and to avoid potential conflict or confidentiality issues, the fiduciary entity should be the client, and the lawyer should have discretion to act in the best interests of the entire situation. If the fiduciary commits a breach, the lawyer thus could disclose this information to the beneficiaries because they would be part of the entity client.

The American Bar Association Real Property, Probate and Trust Section ("ABA Section") takes a traditional approach. According to the ABA Section, the fiduciary is the client and the lawyer has no affirmative duty to inform beneficiaries of impropriety by the fiduciary. If, however, the lawyer decides to withdraw, the manner of withdrawal may signal a warning that something is wrong. The group asked what happens if the beneficiaries do not understand the signal. In that case, the lawyer for the guardian does not represent the ward and cannot reveal the guardian's misappropriation of funds.

Two other treatises consider the fiduciary entity to be the primary client and the fiduciary to be merely the agent of the entity.<sup>2</sup> The duty to a beneficiary, including a ward, derives from the relationship to the entity and requires that the lawyer disclose wrongdoing by the fiduciary. Hazard and Hodes cite an Arizona decision<sup>3</sup> in which the court found that the lawyer for a guardian had a duty to protect the ward from injury by the guardian and that, in fact, "the ward's interests overshadow those of the guardian."

Finally, another commentator, Ronald Link, rejects the entity approach as too problematic and looks to the individual fiduciary as the

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1. See Jeffrey N. Pennell, *Representations Involving Fiduciary Entities: Who is the Client?*, in *Ethical Issues in Representing Older Clients*, 62 *Fordham L. Rev.* 1319 (1994).

2. See Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering: A Handbook on the Model Rules of Professional Conduct* (1990); Geoffrey C. Hazard, Jr., *Triangular Lawyer Relationships: An Exploratory Analysis* (1987).

3. See *Fickett v. Superior Court*, 558 P.2d 988, 990 (Ariz. 1976).

client.<sup>4</sup> Link also places on the lawyer a duty to disclose to both the beneficiary and the court any wrongdoing by the fiduciary against the beneficiary.

### B. Representation

The working group attempted to develop practical answers to complex problems, answers which make sense in everyday situations and which reflect what ought to be rather than what is. Participants considered the relevant Model Rules,<sup>5</sup> the American College of Trust and Estate Counsel Commentaries thereto ("ACTEC Commentaries"),<sup>6</sup> and the cases and ethics opinions cited by Professor Pennell.<sup>7</sup> The participants noted that much of the existing authority on these issues has arisen in the context of disciplinary proceedings against lawyers. The group agreed, however, that the purpose of this symposium was to consider representation of fiduciaries in the context of what will benefit the public and not what is necessary to protect the legal profession from liability. It was the opinion of the working group that, in order to answer the fundamental questions about conflicts and confidentiality, a lawyer must be aware of the boundaries of the representation and his or her obligations within those boundaries.

#### 1. The Client

While all agreed with Professor Pennell that lawyers must "do the right thing," they rejected his theory that the only way to achieve this goal is by representation of the fiduciary entity. Although the group found the entity approach interesting and worthy of discussion, members raised a number of concerns based on the lack of definition of both the client and the lawyer's roles. They asked:

1. How is the entity defined?
2. From whom does the lawyer take direction?
3. How can a lawyer represent a group of people who may have conflicting value systems or interests?
4. What if some members of the entity lack the capacity to participate?
5. How does the lawyer resign?
6. What if the beneficiaries sue the fiduciary?
7. Who can fire the lawyer?

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4. See Ronald C. Link, Significant New Developments in Probate and Trust Law Practice, Developments Regarding the Professional Responsibility of the Estate Administration Lawyer: The Effect of the Model Rules of Professional Conduct (1991).

5. The working group considered the following Model Rules of Professional Conduct: Rule 1.6 on Confidentiality; Rules 1.7 and 1.9 on Conflict of Interest; Rule 1.13 on Organization as Client; and, to a lesser extent, Rule 2.2 on Lawyer as Intermediary.

6. See American College of Trust & Estate Counsel, Commentaries on the Model Rules of Professional Conduct (Oct. 18, 1993) [hereinafter ACTEC Commentaries].

7. See Pennell, *supra* note 1.

8. If the fiduciary fires the lawyer, couldn't the other members of the entity just rehire?
  - a. Would this create a conflict?
  - b. Should it?
9. Doesn't the entity theory just turn the lawyer into a free-floating authority, independent of whoever actually did the hiring?

Some participants were also concerned that the entity theory could not be applied to guardianships, especially guardianships of the person. They queried whether a guardianship of a person, focused on the best interest of an individual ward who may lack capacity to make decisions, can be treated like a trust or decedent's estate, focused on a larger group of persons with competing interests or on a corporation with its board of directors, all of whom are presumed to be competent.

The group considered whether the relationship between the lawyer for the fiduciary and the beneficiary rises to the attorney-client level. The group rapidly determined that it does not, in large part, because of the potential for conflict. Every participant was of the opinion that the lawyer's duties and responsibilities to the beneficiary arise out of the relationship to the fiduciary. Although the group waited to define those duties later in the session, the members agreed that these duties were different from those owed to the fiduciary. The group thus concluded that, without question, the fiduciary should be the client.

To a lesser extent, the group also discussed potential conflicts between the parties to the fiduciary entity and the role of the lawyer with regard to those parties. The group asked with whom the lawyer's loyalties lie if there are multiple fiduciaries who disagree, if the fiduciaries and beneficiaries disagree, or if the interests of two or more fiduciaries are divided. The group asked to what extent conflicts are created when a lawyer represents a fiduciary both as fiduciary and in some other capacity. Finally, the group asked what the lawyer should do in the event of such a conflict.<sup>8</sup>

## 2. Duty

All working group members agreed that the relationship of a lawyer to a fiduciary is different from the typical attorney-client relationship because a fiduciary, in addition to being concerned with his or her own interests, owes a duty to beneficiaries, to third parties, including creditors, and to the court. This led the group to ask several questions:

1. Who are the beneficiaries?
2. Are they only those persons with a direct interest in the actions of the fiduciary?
  - a. In a life estate, for example, are they remainderpersons?
  - b. Are they creditors?

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8. The group considered Model Rules 1.7 and 1.9 in this discussion.

- c. In a guardianship, are heirs or family members of the ward considered beneficiaries?
3. Is there some higher standard of duty in a guardianship, when the direct beneficiary is incapacitated?
4. What about third parties?
5. Does the lawyer become a super-fiduciary, or free-floating authority, who must oversee the fiduciary's actions independent of the person who hired him or her?
6. Does the duty continue if the attorney-client relationship is terminated?

The group agreed that the lawyer is not a super-fiduciary and does not owe the same duty to the entire universe. Like the ACTEC Commentary to Model Rule 1.2, the group decided that the scope of those duties depends upon the "nature and extent of the representation and the terms of any understanding or agreement among the parties." Participants concluded that the lawyer has ancillary duties to the fiduciary, and to other parties where appropriate, such as the duties of good faith, loyalty, due care, diligence, and rightful distribution. Some duties derive from the representation of the fiduciary and include treating the beneficiary with fairness. Some duties are created by public policy, statute, or court rule.

The group moved beyond the ACTEC position, however, and found that, in certain circumstances such as guardianships, the lawyer may be held to higher standards. One participant commented that the fiduciary's actions in guardianships could have greater immediate consequences because the beneficiary's life may be on the line. The group also concluded that, if there is a duty and the relationship which gave rise to that duty is terminated, the duty may continue until it is satisfied.

The ethical dilemma confronting a lawyer who becomes aware that the fiduciary-client is engaged in wrongdoing or, perhaps, in legitimate activity which will harm one or more of the beneficiaries was at the root of the debate. The group asked what, if anything, the lawyer can do to notify the affected parties and if fiduciary representation is different from other practices. Building on earlier discussions, the group concluded that fiduciary representation certainly is different from adversarial practice in that the lawyer for a fiduciary has duties to the non-clients which are unlike any others.

### 3. Confidentiality

The group next discussed whether, under what circumstances, and to whom these duties allow the lawyer to disclose otherwise confidential information concerning the actions of the fiduciary. The group asked:

1. Does disclosure depend on the nature of the actions or of the information?
2. Does the fiduciary have the right to prevent the lawyer from revealing confidential information to the beneficiaries?

Participants suggested several scenarios for discussion:

1. The fiduciary makes a legitimate judgment call which will benefit some persons, but adversely affect others;
2. The fiduciary in some way breaches fiduciary duty;
3. The breach is fraudulent or criminal; and
4. The lawyer discovers that the fiduciary is planning to commit said breach.

The traditional view, as articulated by the ABA Section, is that a lawyer who becomes aware of a breach of responsibility has no duty to notify the beneficiaries but instead has the option to effect a "noisy withdrawal." The group discussed the concept of the noisy withdrawal and concluded that it is not an appropriate way to handle the majority of fiduciary representations. For example, in a trust or probate estate there is at least some chance that the beneficiaries will be able to look out for their own interests. There is little such chance in guardianships, however, where the beneficiary, in all likelihood, does not have the capacity to understand either the reasons for or the process of withdrawal. The group also decided that neither the Model Rules nor the ACTEC Commentaries provide much guidance on the confidentiality issue. While the entity theory allows for disclosures, on the premise that no duties of confidentiality are owed to individuals, the participants decided that this theory raises too many potential problems to be an acceptable answer to this ethical dilemma.

Thus the group concluded unanimously that the lawyer for the fiduciary should not be prohibited from disclosing otherwise confidential information which would negatively impact the beneficiary. The group acted on the assumption that the great majority of lawyers are ethical, practice with care, and require the option of disclosure should the circumstances warrant. The group engaged in lively discussion as to whether disclosure should be mandatory, with one member of the group arguing that it should because of the unique nature of the relationships. This argument did not sway the majority of participants, however, who wanted to give lawyers the option of disclosure without subjecting them to sanctions for failing to do so. There was consensus among the working group that a lawyer for a fiduciary must disclose fraudulent or criminal conduct by the fiduciary of which the lawyer becomes aware with the assumption that, with the mandate, comes the potential for sanctions for non-compliance.

The consensus of the group was that a lawyer should disclose to parties to whom the fiduciary owes a duty, including any beneficiary. The lawyer should also disclose to third parties, such as heirs or creditors, depending upon the circumstances. Understanding that not all fiduciary estates are subject to ongoing supervision by a court, the working group decided that a lawyer should have the leeway to report wrongdoing to any court having jurisdiction.

This decision led the group to ask what the lawyer's responsibility is to supervise the actions of the fiduciary so as to be aware of such conduct.

Trying once again to avoid turning the lawyer into a super-fiduciary who is responsible for all that occurs, the group decided to limit the issue to information of which the lawyer, acting with due care, becomes aware.

#### 4. Communication to the Fiduciary

The group was united in its decision not to look just at what happens when there is a breach of duty by the fiduciary, the default rule, but to examine practical solutions which can help avoid the problem altogether. The group then asked at what point, and in what manner, a client or potential client should be advised of the lawyer's derivative duties to the beneficiary.

As at least a partial solution, the group decided that the lawyer should follow the ACTEC Commentary to Model Rule 1.6 and both should discuss with the fiduciary the respective roles of the fiduciary and the lawyer and should memorialize these roles in writing at the outset of the representation. Participants cautioned that a lawyer should not agree to any limitations on the derivative duties running to a beneficiary as a result of the representation. If potential conflicts arise, these should also be laid out in the letter. While these actions will not resolve all issues of concern, the discussion and writing will provide the client with notice of the lawyer's obligations and, perhaps, will serve as a deterrent to activities which might be subject to disclosure.

Members of the group were interested to learn that it is not universal practice to prepare retainer agreements or letters of engagement, particularly when the lawyer and the client have an ongoing relationship. Some members were concerned that such a writing requirement would impede the smooth development of the attorney-client relationship. The group agreed that a letter of agreement is sound business practice. While it need not be so formal as to set up a barrier, such a writing can explain the nature of the lawyer's role and responsibilities to the fiduciary and to any beneficiaries in a manner which is helpful to both lawyer and client.

### III. RECOMMENDATIONS

The working group did not intend its discussions and conclusions to imply that all fiduciaries engage in wrongdoing, that all beneficiaries are in need of protection, or that a lawyer who represents a fiduciary acting in a fiduciary capacity owes no duties of loyalty or care to the fiduciary client. To the contrary, participants approached their task with the understanding that lawyers are not super-fiduciaries and should not be placed in the difficult position of overseeing every act of the fiduciary. However, participants also recognized that there are special circumstances in fiduciary representation, indeed the very fact that the client is a fiduciary, which merit a high standard of care. They concluded that a lawyer needs guidance on the extent of his or her duties and responsibilities.

At the plenary session, the working group presented its recommendations on interpretations of the Model Rules, practice guidelines, and education. These recommendations evolved from a series of resolutions developed and drafted by the group, as a whole, during the final session. It was the consensus of the group that the issue presented to the plenary session, and the recommendations for implementation, should incorporate the fundamental principles developed during the two intense days of discussion. Unfortunately, the group did not have sufficient time to address the conflict questions beyond a recognition that, in their current form, Model Rules 1.7 and 1.9 are not particularly applicable to fiduciary situations. The group recommended these issues for further study.

In conclusion, the group drafted and passed the following resolutions, upon which they based their recommendations presented at the plenary session:

A. That the lawyer for a fiduciary, acting in any fiduciary capacity, *may* communicate otherwise confidential information to any court having jurisdiction, and to parties to whom the fiduciary owes duties.

1. Minority View

That the lawyer has an obligation to communicate confidential information if the lawyer becomes aware of criminal actions by the fiduciary.

B. That the fiduciary is the client, not the beneficiaries. The lawyer has derivative duties to the beneficiaries as a result of the representation of the fiduciary. Disclosures relating to those duties are impliedly authorized in order to carry out the representation. *See* Model Rule 1.6(a).

C. That this issue be clarified by court rule.

D. That this group has rejected the entity theory.

E. That Model Rules 1.7 and 1.9 are not well-suited to fiduciary representations where there is no adversity, and in which the lawyer represents more than one interest. For example, can a lawyer represent co-fiduciaries, or a fiduciary and a beneficiary?

F. We recommend further study with regard to the Rules' application to these conflict situations.

G. That it is good practice to discuss with the fiduciary the respective roles and responsibilities of both the lawyer and the fiduciary, and to memorialize these roles in writing. The lawyer should not agree with the fiduciary to any limitations on derivative duties to the beneficiary.

H. That educational materials describing the duties and responsibilities of fiduciaries and their lawyers should be developed for the guidance of the bench, bar, and fiduciaries.<sup>9</sup>

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9. For the full text of the Recommendations of this working group, see Conference on Ethical Issues in Representing Older Clients, *Recommendations, in* Ethical Issues in Representing Older Clients, 62 Fordham L. Rev. 989 (1994).

