Trustee Liability and Exposure

We frequently receive questions from individuals who have been asked to, or are currently acting as, a Trustee. The most frequent question is in regards to coverage for these services under their (accountants) professional liability policy.

Although each policy form is different, it is our opinion that most accountants professional liability policies intend to provide coverage for an accountants professional services as a Trustee. *Only your actual policy form can confirm the coverage, conditions, and exclusions relevant to your firm.*

There are two key areas in your policy to review for confirmation of coverage.

Definition of Professional Services

The preference is that the policy specifically states coverage for services as a Trustee.

i.e. – Professional includes; *services performed by any INSURED as a TRUSTEE, RECEIVER or EXECUTOR*;

Other policies may encompass coverage under a broader definition of professional services.

i.e. - **Professional Services** means services performed or advice given by **you** to others provided that the remuneration for such services or advice, or a portion thereof, inures to **your** benefit.

Although not specifically including Trustee in the policy wording, the intent is clear enough that such services would be included in services performed by you for remuneration.

Exclusions

Even if coverage is appears to be afforded in one section of a policy form, it is essential to review all policy exclusions, including endorsements. Exclusions and endorsements may override coverage even if affirmatively provided under a policy definition or condition.

The common exclusion relevant to Trustee services is intended to void coverage where there is a potential conflict of interest.

i.e. – (This policy does not apply to claims) based upon, arising out of or brought by or on behalf of a trust or estate if **you** are a beneficiary or distributee.

This is an acceptable exclusion as it excludes coverage for your services as a Trustee only if there is an inherent conflict of interest based on your participation as a beneficiary of the trust.

What is the exposure of a Trustee?

To answer this question it is beneficial to understand the role of a Trustee. A Trustee is a fiduciary put in charge of overseeing the management of property (land, securities, property, currency, etc.) owned by a trust. A Trustee can be an individual, an institution, such as a bank or trust company, or a combination of both. The exact duties of a Trustee will vary based on what assets are owned by the trust.

As a fiduciary, a trustee must act solely in the best interests of the trust.

The Trustee can, depending on state law and the terms of the trust agreement, delegate certain duties to others, such as hiring a financial advisor to oversee investments or hiring a property manager to oversee rental real estate. But the Trustee must use good judgment and due diligence when delegating duties and must also avoid any conflicts of interest (such as hiring a sibling as the trust's investment advisor) unless the beneficiaries consent.

Trustee Liability Claim Examples

Accepting the role of a Trustee should not be taken lightly. As with all professional services, there are exposures and liabilities inherent to the role of a Trustee. Understanding these exposures will assist you in developing appropriate risk management strategies to mitigate such exposure.

The following actual claim summaries provide actual examples of potential exposures faced by Trustees.

1. A trust's assets declined significantly due to decisions made by the trust's investment advisor. The trustee was sued for failure to properly select and supervise the investment advisor, for failure to ensure that the assets were invested in accordance with the trust's objectives, and for negligence in tax planning. The case was finally settled after protracted litigation.

2. A trust reduces its annual contribution to a charitable beneficiary. The charity begins an investigation, and determines that the trust has begun making contributions to other charities. It brings an action against the trustee, claiming that its distributions have been wrongly diverted to other organizations. It also brings an action against the law firm that wrote the trust document, claiming its drafting negligence deprived the charity of millions. The litigation is on-going.

3. A family office provided services to a number of family trusts. One trust was offered an opportunity to sell shares it owned back to the company at market prices; the other trusts were not offered the same opportunity. On advice of counsel, the family office sold the shares back, and did not extend the offer to the other trusts (it may not have had the right to). Subsequently, the price of the stock fell dramatically, costing the other trusts substantial losses. Beneficiaries of these trusts brought an action claiming breach of fiduciary duty for not extending the buy-back offer. The action went to trial, and the defendants won. However, legal expenses exceeded $1.0 million.

4. A family trust has a range of assets, but the most significant asset is a private company. The company is put up for sale and sold to a group of investors. The group is not the highest bidder, but has the most solid financing plan. A small beneficiary of the trust is a non-profit organization, which will benefit from on-going distributions by the trust from the sale of the company. The State Attorney General begins an investigation of the sale, and brings an action against the trustee for failure to accept the highest bid for the company. The Attorney General has a right of action because of the non-profit beneficiary.

5. A trustee desires to diversify the trust's assets, and puts some of the funds into a large, well-known mutual fund. Subsequently, the mutual fund sustains significant investment losses. An action is brought by the beneficiaries against both the trustee and the advisor for failure to follow prudent investment guidelines and failure to invest in accordance with the trust's objectives. After months of discovery, the case settles to avoid continued escalation in defense costs.

Risk Management Steps

The following items are some potential risk management steps that you may consider adapting to your individual scenario.

1. **Indemnification** – when possible, have the trust indemnify the Trustee from suits, other than negligence

2. **Certificates of Insurance** – make sure that all other professionals (especially investment advisers) retained on behalf of the trust maintain errors & omissions insurance.

3. **Direct access to Funds** – as a Trustee you should not have direct access to funds. Create a holding account where funds can be transferred to for necessary bill paying, and other actions.

4. **Trustee Liability Insurance** – if it is a large trust, consider purchasing a stand-alone Trustee liability policy. Although not inexpensive, payment for the premium may be made by the trust if included in the trustee agreement.

5. **Payment** – How are you paid? Your Errors & Omissions policy provides coverage for you firm. If you are paid individually by the trust you should contact your insurance agent about being added as an additional named insured to your Errors & Omissions policy.

6. **Trustee Duties** – similar to an engagement letter, the trustee agreement should be detailed in the specific duties of the Trustee. In addition, it is beneficial to outline those areas that the Trustee is not responsible for.