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Ariz. R. Crim. P. 31.24



DIVISION ONE
FILED: 09/18/2012
RUTH A. WILLINGHAM,
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IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

In the Matter of:) No. 1 CA-CV 10-0673
)
THE RESIDUARY TRUST UNDER THE)
LAST WILL AND TESTAMENT OF) DEPARTMENT E
CLAUDE L. HUBBARD, DATED)
07/11/1988; and THE HUBBARD)
FAMILY TRUST UNDER AGREEMENT)
DATED NOVEMBER 16, 1989.) **MEMORANDUM DECISION**
_____))
) (Not for Publication -
BRUCE A. PENNELL, an individual;) Rule 28, Arizona Rules of
BETH A. PENNELL, an individual;) Civil Appellate Procedure
ANDREW J. ALVERSON, an)
individual; PHILIP PENNELL, as)
representative of the Estate of)
Geraldine Pennell,)
)
Plaintiffs/Appellants,)
)
v.)
)
ANGELLA ALVERSON, individual and)
Trustee,)
)
Defendant/Appellee.)
_____)

Appeal from the Superior Court in Maricopa County
Cause Nos. CV2006-006746/PB2005-003541 (Consolidated)

The Honorable Karen L. O'Connor, Judge

AFFIRMED IN PART; VACATED IN PART; REMANDED

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J O H N S E N, Judge

¶1 Philip Pennell, as the personal representative of the Estate of Geraldine Pennell, and Bruce A. Pennell, Beth Pennell and Andrew J. Alverson (collectively, the "Opposing Beneficiaries") appeal the superior court's judgment in favor of Angella Alverson on their claims arising out of her actions as Trustee of the Hubbard Family Trust Agreement dated November 16, 1989. For the following reasons, we affirm in part, vacate in part and remand.

FACTS AND PROCEDURAL BACKGROUND

¶2 Claude and Cleo Hubbard had two daughters, Geraldine Pennell and Kathleen Alverson, and six grandchildren, Bruce and Beth Pennell and Angella, Annette, Amelia and Andrew Alverson.¹ In 1988, Claude executed a will that contained a testamentary trust (the "Claude Trust"). Cleo was the sole income and principal beneficiary of the Claude Trust during her lifetime,

¹ After Geraldine's death, her husband, Philip Pennell, was appointed the personal representative for her estate.

and the remainder beneficiaries were their daughters and grandchildren. The Claude Trust named Cleo and Angella as co-Trustees. Claude died in 1991, and the funding of the Claude Trust was authorized by court order in 1998.

¶13 In 1989, Cleo executed a Declaration of Trust (the "Cleo Trust"). As relevant, it provided that Cleo was the sole income and principal beneficiary of the Cleo Trust during her lifetime, and the remainder beneficiaries were Cleo's daughters and grandchildren. The Cleo Trust provided, however, that Angella "shall not share in any of this trust until all of the other beneficiaries shall have received \$300,000.00. After that amount has been allocated to the other beneficiaries, if there are enough funds in the trust to do so, then she shall share, share and share alike in any excess amount." The Cleo Trust named Cleo as Trustee and Angella as successor Trustee, in the event of Cleo's death or resignation.

¶14 In 1990, Cleo executed an amendment to the Cleo Trust (the "First Amendment"), which provided that upon Cleo's death, the trust would be distributed to her beneficiaries in equal shares, "except, that [Angella's] share shall be reduced by any indebtedness owing to [Cleo]." The amendment also expressly reserved the settlor's right to amend or revoke the trust. In 1993, Cleo again amended the Cleo Trust (the "Second Amendment") to appoint Angella as co-Trustee effective July 7, 1993. The

Second Amendment also provided: "Effective July 1, 1993, [Angella] has repaid all indebtedness to [Cleo]. Therefore, the said share allocated for the benefit of [Angella] shall not be reduced."

¶15 Cleo died on February 24, 2002. In 2003, Angella provided all of the remainder beneficiaries with an accounting for both the Claude Trust and the Cleo Trust. Thereafter, in response to questions raised by the Pennells, Angella agreed to allow an independent auditor selected by the Pennells to examine the accounting records of the Cleo Trust. The auditor concluded he found nothing unusual or any transactions that appeared to constitute a breach of fiduciary duty.

¶16 Angella then filed a petition for approval of her proposed distribution of the trust assets and asked the court to award her compensation for her service as Trustee. The Opposing Beneficiaries objected to the petition and filed a complaint against Angella, individually and in her capacity as Trustee, alleging breach of fiduciary duty, breach of trust agreement, constructive fraud, conversion, negligence and failure to account for trust property. The complaint also sought a declaratory judgment that the Second Amendment was void and the removal of Angella as Trustee.

¶17 The case was tried to the court. After the Opposing Beneficiaries presented their case-in-chief, Angella moved to

dismiss the claims in the complaint insofar as they were based on alleged acts that occurred prior to Cleo's death. Angella argued that until Cleo died, she owed a fiduciary duty as co-Trustee only to Cleo, not to the remainder beneficiaries. The court granted the motion. It ruled that because the Cleo Trust was a revocable trust, Angella had no fiduciary duty to the Opposing Beneficiaries during Cleo's lifetime pursuant to Arizona Revised Statutes ("A.R.S.") section 14-10603 (West 2012).²

¶8 The remainder of the trial focused on the Opposing Beneficiaries' allegation that in 2003 Angella improperly distributed stock to herself and deprived the Cleo Trust of a tax benefit. The court found Angella had not breached her fiduciary duty by making the distribution, but ordered her to reimburse the Cleo Trust for the tax benefit it would have received if it had retained the stock. The court further found in Angella's favor on the Opposing Beneficiaries' declaratory relief, negligence, constructive fraud and conversion claims. In addition, the court granted Angella's request for compensation for her role as Trustee, including reasonable attorney's fees and costs incurred in defending herself in the action, whether individually or in her capacity as Trustee.

² Absent material revisions after the relevant date, we cite a statute's current version.

¶9 The Opposing Beneficiaries timely appealed the judgment. We have jurisdiction pursuant to A.R.S. § 12-2101(A)(9) (2011).

DISCUSSION

¶10 We review the superior court's legal conclusions *de novo*, but will not set aside its findings of fact unless they are clearly erroneous. *In re Estate of Zaritsky*, 198 Ariz. 599, 601, ¶ 5, 12 P.3d 1203, 1205 (App. 2000).

A. Dismissal of Claims Based on Angella's Acts Prior to Cleo's Death.

¶11 The superior court granted judgment for Angella at the conclusion of the Opposing Beneficiaries' case-in-chief on the Opposing Beneficiaries' claims insofar as they were based upon Angella's actions prior to Cleo's death.

1. Breach of fiduciary duty to the Opposing Beneficiaries.

a. Choice of law.

¶12 Arizona law provides that the meaning and effect of the terms of a trust are determined by the law of the jurisdiction designated in the trust instrument. A.R.S. § 14-10107(A) (Supp. 2010). Further, "[i]n the absence of a controlling designation in the terms of the trust, the laws of the jurisdiction where the trust was executed determine the validity of the trust, and the laws of descent and the law of

the principal place of administration determine the administration of the trust." A.R.S. § 14-10107(B).

¶13 The Cleo Trust contains a provision that states: "The powers and duties of the Trustee hereunder involving all questions of interpretation of this instrument shall be governed by the laws of the State of Michigan." Although perhaps not artful, we construe this provision to mean that Michigan law controls the interpretation of the trust concerning the powers and duties of the Trustee.

¶14 The Opposing Beneficiaries argue that because the trust provided that Michigan law would control questions relating to the duties of the Trustee, the superior court erred by applying A.R.S. § 14-10603 to dismiss their claim for breach of fiduciary duty based on acts Angella allegedly committed before Cleo's death.³ Citing a Michigan statute, Mich. Comp. Laws Ann. § 700.7105 (West 2012), they argue that under Michigan law, the terms of a trust prevail over statutory provisions governing the duties and powers of a trustee. The Michigan statute they cite states that, with certain exceptions not relevant here, "the duties and powers of a trustee . . . and the

³ The Arizona statute states: "While a trust is revocable by the settlor, the rights of the beneficiaries are subject to the control of, and the duties of the trustee are owed exclusively to, the settlor."

rights and interests of a trust beneficiary" will be governed by any applicable "terms of the trust."

¶15 We agree with the Opposing Beneficiaries that Michigan law applies to questions relating to the Trustee's duties under the trust. Nevertheless, as explained below, we conclude the Cleo Trust did not impose on Angella a fiduciary duty owed to the Opposing Beneficiaries during Cleo's lifetime.

b. Whether the trustee owed a fiduciary duty to the Opposing Beneficiaries.

¶16 The Opposing Beneficiaries argue Section 4(F)(1) of the Cleo Trust imposed on the Trustee a fiduciary duty to them at all times, including during Cleo's lifetime. That language provides:

Trustee may freely act under all or any of the powers by this agreement given to them in all matters concerning the trust herein created, after forming their judgment based upon all the circumstances of any particular situation as to **the best course to pursue in the interest of the trust and the beneficiaries hereunder**, without the necessity of obtaining the consent or permission of any person interested therein, or the consent or approval of any court. Trustee may so act notwithstanding that they may also be acting individually, or as Trustee of other trusts, or as agent for other persons or corporations interested in the same matters, or may be interested in connection with the same matters as stockholder, director, or otherwise. However, **Trustee shall exercise such powers at all times in a fiduciary capacity primarily in the interest of the beneficiaries hereunder.**

* * *

Trustee shall have the power to do all acts, institute all proceedings, and exercise all rights, powers and privileges that any absolute owner of the trust property would have, **subject always to the discharge of Trustee's fiduciary obligations.**

(Emphasis added.)

¶17 Under Michigan law, we examine the language of the trust to determine Cleo's intent and only consider information outside the document (the surrounding circumstances and the rules of construction) if we find a patent or latent ambiguity. *Matter of Maloney Trust*, 377 N.W.2d 791, 793 (Mich. 1985).

¶18 The language the Opposing Beneficiaries rely on is in the section of the trust entitled "Specific Powers of Trustee," which is a subsection of a section titled "Powers and Duties of Trustee." That subsection explicitly allows the Trustee to freely exercise all powers given to her by the trust, even in matters for which she has a competing interest, so long as she acts at all times in her fiduciary capacity "primarily in the interest of the beneficiaries" under the Cleo Trust.

¶19 Contrary to the Opposing Beneficiaries' argument, this provision does not establish that, as Trustee, Angella owed a fiduciary duty to the remainder beneficiaries during Cleo's lifetime. Cleo was the original Trustee of the Cleo Trust, and until her death, she continued to be co-Trustee after Angella's

appointment as co-Trustee by virtue of the Second Amendment to the trust. Therefore, when we construe the Cleo Trust's provisions pertaining to the duties of the Trustee, we must adopt an interpretation that sensibly and logically may be applied both to Cleo and Angella as Trustees and as co-Trustees. At the same time, we must recognize that while she lived, Cleo not only was Trustee of the Cleo Trust, she also was a beneficiary of the Trust. Viewed from these competing perspectives, the Opposing Beneficiaries' contention that as Trustee, Angella owed them a fiduciary duty during Cleo's lifetime cannot stand.

¶20 We come to this conclusion by examining the settlor's power to amend or revoke the Cleo Trust, which Cleo reserved for herself. While the trust is not a model of clarity, it contains language from which we conclude that as settlor, Cleo reserved the right to amend or revoke the trust. She did so by providing in the Cleo Trust that the trust property would be held and administered "under the terms and provisions of this declaration of trust *and any amendment or modification hereof.*" (Emphasis added).

¶21 Although the Opposing Beneficiaries argue that Cleo did not intend to reserve the right to amend or revoke the trust, the undisputed evidence was that Cleo twice amended the trust. Indeed, in the First Amendment to the trust, executed

just 10 weeks after the original trust instrument, Cleo expressly provided, "Grantor may at any time or times, during the lifetime of the Grantor, by instrument in writing delivered to the Trustee, amend or revoke this agreement in whole or in part." From this there can be no doubt that it was Cleo's understanding and intent that the Cleo Trust was revocable and subject to amendment. See Restatement (Second) of Trusts § 330 (1959) ("settlor has power to revoke the trust if and to the extent that by the terms of the trust he reserved such a power"), cmts. a & b (power to revoke a trust need not be expressly contained in the written words of the trust document; when a settlor's intention to alter the trust may be proved by competent evidence, it becomes a term of the trust whether it is expressed by written or spoken words or by conduct).

¶22 Our conclusion, moreover, is consistent with the position that the Opposing Beneficiaries took at trial, where they repeatedly conceded that Cleo had the right during her lifetime to revoke the trust or to change or eliminate the beneficiaries.

¶23 By reserving the right to alter the Cleo Trust, Cleo implicitly reserved the right to change or eliminate the remainder beneficiaries. Yet under the Opposing Beneficiaries' argument, both Cleo and Angella, as Trustees, owed a fiduciary duty to the beneficiaries of the trust to prevent such an

amendment or revocation. We cannot see how the trust document sensibly could impose on Cleo, as Trustee, a fiduciary duty to the Opposing Beneficiaries when, in creating the trust, she reserved for herself the power to amend or revoke the trust, presumably including the right to modify the trust terms to eliminate the interests of one or more of the Opposing Beneficiaries. In short, the power to amend or revoke the trust that Cleo reserved for herself as settlor cannot be reconciled with the purported fiduciary duty that the Opposing Beneficiaries argue she owed to them as Trustee. By the same token, we cannot accept the Opposing Beneficiaries' argument that as Trustee, Angella had a fiduciary duty to the remainder beneficiaries to somehow restrain Cleo's exercise of her power to amend or revoke the trust.

¶24 For these reasons, we conclude the Cleo Trust did not impose on Angella a fiduciary duty to the Opposing Beneficiaries during Cleo's lifetime. To the contrary, we conclude that the only sensible construction of the Cleo Trust is that the language imposing a fiduciary duty to the beneficiaries must refer to an obligation owed to the beneficiaries that commenced only after Cleo's death.

¶25 The Opposing Beneficiaries, however, argue that under Michigan law, a revocable inter vivos trust imposes on the trustee a fiduciary duty to a remainder beneficiary. Although

Michigan courts have recognized that a remainder beneficiary has an expectancy interest and that a trustee may owe a duty to such a beneficiary, the overarching rule we can discern from the Michigan cases is only that the language of the trust instrument controls. See *In re Estate of Butterfield*, 341 N.W.2d 453, 461 (Mich. 1983) ("The law is well established that one must look to the trust instrument to determine the powers and duties of the trustees and the settlor's intent regarding the purpose of the trust's creation and its operation.")

¶26 The only authority the Opposing Beneficiaries cite that concerned a situation similar to the one in this case is *Sabin-Scheiber v. Sabin*, 340 N.W.2d 114 (Mich. App. 1983). In that case, a woman established a trust and named herself, her husband and her son as co-trustees. *Sabin*, 340 N.W.2d at 115. She was the lifetime beneficiary of the trust; her son and other descendants were the remainder beneficiaries. *Id.* After she became mentally incompetent, her husband removed money from the trust and deposited it in an account held jointly by him and their son, then used the funds to pay for the woman's care. *Id.* After she died, the other descendants filed a complaint against the son. *Id.* The Michigan court of appeals affirmed the lower court's verdict in favor of the son. *Id.* at 117.

¶27 The Opposing Beneficiaries argue that in affirming the lower court's holding, the court of appeals impliedly held that

a trustee owes a fiduciary duty to remainder beneficiaries during the lifetime of the settlor. As described by the Michigan court, however, the issue in that case was not any duty the son allegedly owed to the remainder beneficiaries during the settlor's lifetime. Instead, the issue was whether the son breached a fiduciary duty to the woman during her lifetime and breached a duty to the remainder beneficiaries after her death. *Id.* at 115.⁴

¶28 The Opposing Beneficiaries cite cases from other jurisdictions that they argue support their contention that Angella owed a fiduciary duty to them during Cleo's lifetime. The cited cases do not present facts such as are present here. In the absence of authority on point, we are reluctant to adopt the Opposing Beneficiaries' argument that a Michigan court would impose an inter vivos duty to the remainder beneficiaries on the circumstances of this case. Accordingly, the superior court did not err by dismissing the Opposing Beneficiaries' claim for breach of fiduciary duty based on alleged acts by Angella prior to Cleo's death.

⁴ The court observed, "On appeal plaintiffs argue that defendant was under a fiduciary obligation to administer the assets of the two trusts for the benefit of the settlors and the children of the settlors after their deaths." *Id.*

2. Other claims.

¶29 In Count Two of their complaint, the Opposing Beneficiaries alleged Angella breached the trust agreement by breaching her fiduciary duties as Trustee and by mismanaging trust assets. Count Four of the complaint alleged Angella committed constructive fraud, *inter alia*, when she failed to disclose to Cleo that she allegedly was not qualified to serve as Trustee and by falsely representing in the Second Amendment to the Cleo Trust that her debt to the trust had been repaid. In Count Five, which alleged conversion, the complaint alleged that Angella "wrongfully exercised ownership and control over" trust property, and in Count Six, the complaint alleged that Angella negligently breached her duty to exercise care and reasonable diligence in handling trust property.

¶30 The superior court dismissed each of these claims at the close of the Opposing Beneficiaries' case-in-chief insofar as they were based on alleged acts by Angella prior to Cleo's death. The parties' trial memoranda filed in connection with Angella's oral motion to dismiss focused for the most part on the Opposing Beneficiaries' breach-of-fiduciary-duty claim and did not address their other claims in any detail. In its minute entry granting the motion, the court did not set out the rationale for its decision to dismiss the other claims.

¶31 On appeal, Angella argues the dismissal of all the claims was proper for the same reason the court correctly dismissed the fiduciary duty claim against her for actions taken prior to Cleo's death - she owed no fiduciary duty to the Opposing Beneficiaries before Cleo's passing. Angella argues the Opposing Beneficiaries therefore lack standing to state a claim for breach of the trust agreement.

¶32 We are not certain that the other claims are barred as a matter of law by the superior court's correct conclusion that Angella owed no fiduciary duty to the Opposing Beneficiaries during Cleo's life. There is no dispute that from the time Angella was appointed co-Trustee, she owed a fiduciary duty to Cleo as settlor. She also owed a duty to Cleo to comply with the terms of the trust agreement. In their reply brief on appeal, the Opposing Beneficiaries suggest that, like the remainder beneficiaries in *Sabin-Scheiber*, they have standing to sue for breaches of duties Angella owed to Cleo during Cleo's lifetime. See, e.g., *Brundage v. Bank of America*, 996 So.2d 877 (Fla. App. 2008); *Smith v. Bank of Clearwater*, 479 So.2d 755 (Fla. App. 1985).

¶33 We do not resolve that issue, however, because we cannot discern from the record the basis of the superior court's decision to enter judgment in favor of Angella on the other claims. Perhaps the court found that the evidence offered by

the Opposing Beneficiaries in their case-in-chief was insufficient to prove a breach. In that case the only issue on appeal would be whether the evidence supported the court's conclusion. On the other hand, the court's order of dismissal cited only A.R.S. § 14-10603 and its conclusion that Angella "had no fiduciary duty" to the Opposing Beneficiaries for as long as Cleo lived; perhaps that legal conclusion was the sole basis for its ruling. We agree that Angella owed no fiduciary duty to the Opposing Beneficiaries during Cleo's lifetime, although we come to that conclusion by applying Michigan law, not Arizona law. The question of standing for which the Opposing Beneficiaries cite *Sabin-Scheiber* arises only if the superior court decided that the evidence might establish a breach by Angella of the duties she owed Cleo during Cleo's life, but then concluded that the Opposing Beneficiaries cannot pursue such a claim because Angella owed them no duty during Cleo's life.

¶34 Because we cannot discern the basis for the court's dismissal of Counts Two through Six insofar as they were based on acts that occurred prior to Cleo's death, we vacate and remand the order of dismissal of those claims for further proceedings.

B. Dismissal of Claims Based on Alleged Acts After Cleo's Death.

¶35 The superior court also heard evidence on the Opposing Beneficiaries' claims based on alleged wrongdoing by Angella after Cleo's death relating to the manner in which she arranged for the distribution of funds to the eight beneficiaries in 2003.

¶36 The evidence showed that in January 2003, Angella made a \$25,000 distribution to each of the remainder beneficiaries of the Cleo Trust, including herself. She distributed cash to all of the other beneficiaries, but took her distribution in a combination of cash and stock. The stock Angella received from the trust had depreciated in value and she benefited from a capital loss. Thereafter, the Cleo Trust sold additional stock and, had it retained the stock distributed to Angella, it would have benefitted from the capital loss because its tax liability would have been reduced by \$16,668.74.

¶37 Angella testified she followed professional tax advice concerning the distribution and at the time of the distribution she did not anticipate that the Cleo Trust would be able to claim the benefit of a capital loss. The superior court determined Angella did not breach her fiduciary duty by taking a portion of her distribution in stock, but ordered her to repay the trust \$16,668.74.

¶38 The Opposing Beneficiaries offer no argument on appeal why the court might have erred by dismissing all of their claims insofar as they are based on the 2003 stock events. The superior court's determination is not clearly erroneous. *Spaulding v. Pouliot*, 218 Ariz. 196, 199, ¶ 8, 181 P.3d 243, 246 (App. 2008).

C. Individual Liability of the Trustee.

¶39 The Opposing Beneficiaries also argue the superior court erred in determining that their claims against Angella arose solely out of her status as Trustee of the Cleo Trust, and not against her individually. However, as one of the Opposing Beneficiaries acknowledged at trial, all of the claims involved wrongful acts that Angella allegedly committed in her capacity as Trustee. Accordingly, we find no error.

D. Attorney's Fees and Trustee Compensation.

¶40 The Opposing Beneficiaries argue the superior court erred in ordering that trust funds be used to pay the attorney's fees Angella incurred defending herself against the Opposing Beneficiaries' claims. Arizona law provides that a trustee is entitled to reimbursement from the trust for reasonable attorney's fees and costs that "arise out of and that relate to" proceedings involving the administration of the trust. A.R.S. § 14-11004(A) & (B) (West 2012). Nevertheless, because we have in part vacated the superior court's judgment in Angella's favor,

we vacate its order granting her attorney's fees. For the same reason we vacate the superior court's award of Angella's compensation. See A.R.S. § 14-10708 (Supp. 2010); *In re Dunlap's Estate*, 38 Ariz. 525, 530, 2 P.2d 1045, 1046-47 (1931). The court may reconsider Angella's requests for fees and compensation at the conclusion of the matter.

CONCLUSION

¶41 For the foregoing reasons, we affirm the superior court's judgment in part, vacate it in part, and remand for further proceedings consistent with this decision. We deny without prejudice Angella's request for her attorney's fees and costs on appeal pursuant to A.R.S. § 14-11004(A) and (B). On remand, she may ask the superior court to award her fees and costs incurred in this appeal at the conclusion of the matter. Because the Opposing Beneficiaries have prevailed on appeal, we grant their request for costs, conditioned on compliance with Arizona Rule of Civil Appellate Procedure 21.

/s/
DIANE M. JOHNSEN, Presiding Judge

CONCURRING:

/s/
PATRICIA A. OROZCO, Judge

/s/
PATRICIA K. NORRIS, Judge