

STATE OF MICHIGAN
COURT OF APPEALS

In the Matter of WILLIAM M. REID TRUST.

FERN REID AND RANDY REID,

Petitioners-Appellants,

v

LEONARD PALIS,

Respondent-Appellee.

UNPUBLISHED

February 23, 1999

Nos. 202537; 204552

Macomb Probate Court

LC No. 89-111457 TI

Before: Whitbeck, P.J., and Cavanagh and Griffin, JJ.

PER CURIAM.

Petitioners appeal the probate court's orders denying their request to surcharge respondent Leonard Palis as trustee of the William M. Reid Trust (the "Trust") and awarding Palis fiduciary fees, in addition to authorizing the payment of attorney fees from trust proceeds for legal services rendered on behalf of the Trust. We affirm.

I. Basic Facts And Procedural History

Following William M. Reid's death in 1989, Palis became the successor trustee of the Trust. Perhaps not coincidentally, Palis had been Reid's accountant for forty years. Prior to his death, Reid became involved with a company named Applied Industries ("Applied"). Originally, Reid loaned Applied money for operating capital. When Applied ran into financial difficulties, Reid asked Palis to review the situation and, in 1982, both Reid and Palis began investing their money in Applied.

At the time of Reid's death, the Trust possessed a promissory note from Applied in the amount of \$555,000 and 66,389 shares of stock in Applied. Palis personally possessed a promissory note of approximately \$500,000 at the time of Reid's death, because he and Reid had been making matching contributions. Whenever Applied needed additional money, Palis and Reid invested more of their personal finances into the company and, in fact, Palis invested most of his trustee payments back into

the company. Palis held a position on Applied's board as an officer in the company, serving as the vice president and treasurer.

Palis testified that in 1982 he and Reid effectuated a UCC filing to secure repayment of their promissory notes. However, Palis was not aware that the UCC filing was only effective for five years and the UCC filing expired in May 1987. Reid never instructed Palis to renew the UCC financing statement prior to Reid's death in 1989. In fact, Palis also failed to renew his own financing statement. Believing that both notes were secured by the UCC filing, Palis did not seek to perfect Reid's promissory note as a secured claim for the benefit of the Trust.

Between 1986 and 1988, Applied realized a net loss each year. In an effort to reduce costs, Applied decided to move its operations to a smaller location with cheaper rent. The new location was a building owned by Palis and his partner, Charlie Baer. Reid knew that Palis was a part owner of the new building, and he was in favor of the move. Baer's and Palis's mortgage payment on the new building was \$3,000, the same amount charged to Applied as monthly rent. Palis testified that the rent charged for the new building was well below fair market value.

Applied owned some of its own equipment and leased the rest. When Applied needed a "Fidell" machine to make operations more productive and profitable, it was unable to obtain the necessary financing. However, Palis was able to finance the machine, through his company WRP Investment, and he then leased it to Applied. As with the rent for the new building, Palis testified that he made no profit on the lease. Applied entered into the lease agreement with Palis prior to Reid's death, and Reid was aware of the lease arrangement.

In addition, Applied hired Palis's accounting firm to keep its books. Palis's firm charged Applied \$2,000 a month for accounting services. According to Palis, the accounting fees were reasonable and necessary. Palis testified that he believed that he probably billed for only half of the hours that he actually worked on behalf of Applied.

After Reid's death, Palis hired a probate specialist to assist with the preparation of the tax return relating to the assets contained in the Trust. The tax return reflected that 66,389 shares of Applied's stock were held by the Trust. The return also revealed that Applied was insolvent. The return estimated the value of the stock in Applied to be fifty cents a share. Further, the return revealed that the chances for repayment on the promissory note from Applied were only about 50%, based on the poor financial condition of Applied. However, Palis testified that he believed that he could still help Applied become profitable and, in 1990, Applied made a profit of \$39,000. During the same year, Applied completed nineteen prototype, two-and-a-half ton trucks in an effort to be awarded with a contract to build a truck for a joint venture between General Motors and BMW. However, approximately a year and a half later, Palis was informed that the contract was awarded to another company and after 1990 Applied never made a profit.

Prior to Reid's death in 1989, Palis had a 20% ownership interest in Applied. After two conversions in 1989 and 1990, in which Palis converted part of his promissory note into capital stock,

Palis had a 56.7% ownership interest in Applied and by the time of the board's annual meeting for fiscal 1993, Palis owned 56.7%, Baer owned 7.88%, and the Trust owned 10.46% of the stock of Applied.

At the annual meeting, the board granted security interests in their machinery for past and future rent and for the accounting services to Baer, Palis and "Palis & Company"; however, the security agreement was never filed or acted upon. The board decided to order the liquidation of Applied and to file either a Chapter 11 or Chapter 7 bankruptcy petition; however, Palis did not advise petitioners of this action. A new board of directors was elected which consisted only of Palis and Baer.

Subsequently, Palis wrote a letter, dated December 30, 1993, to the board demanding payment of the promissory notes issued to himself and the Trust. Further, an eviction notice was sent to the board for unpaid rent. A special meeting of the board was held on February 1, 1994, and the board decided to liquidate the corporation and transfer all assets to the secured creditors, the Trust and Palis, because of their demand for payment of the promissory notes.

In July 1994, Applied's assets were sold and converted into cash. Palis had an auctioneer appraise Applied's machinery and equipment. Another company, Ultimate Hydroforming, knew Applied was about to shut down and offered to match the auctioneer's estimate in exchange for the equipment and machinery, and Applied ultimately sold its equipment and machinery directly to Ultimate Hydroforming for \$155,000. Through this direct sale, Applied avoided the commission fees associated with conducting an auction. With the proceeds from the sale of the machinery and equipment, Palis paid Applied's personal property taxes and rent, and split the remainder between himself and the Trust. On November 9, 1994, an involuntary petition for bankruptcy was filed by Applied's judgment creditor.

In November of 1994, petitioners filed a complaint in Macomb County Probate Court seeking to preserve the assets of the Trust and requesting that the probate court surcharge Palis for his "maladministration" of the Trust. In response, Palis requested that the estate pay for attorney fees incurred on its behalf and pay him for his fiduciary fees and professional accounting fees. Following a hearing, the probate court issued a written opinion on December 16, 1996, stating:

The hearing on the accounts provided no evidence of any damages incurred by the Reid enterprises. On the contrary, the uncontested testimony indicated valid reasons for the activity of the trustee. The collection on the note may force problems or bankruptcy and jeopardize the efforts to obtain the government contract. The accounting work and rental of machinery and building were at or below market value. It is further noted that these transactions were reviewed by the bankruptcy court without any detrimental consequences. [Appendix E, p 3.]

According to the probate court, Palis helped Applied avoid bankruptcy and reduced the amount of estate taxes. The probate court found that by placing Applied in a bankruptcy proceeding, Palis would have subjected Applied and the Trust to the claims of perfected creditors. The probate court determined that Palis did not act any less than a prudent person while he made decisions as trustee. Furthermore, the probate court determined that Palis did not exhibit bad faith or gross negligence. While the probate court stated that a fiduciary who works in a dual capacity walks in harm's way, it

noted that the law does not specifically prohibit working in a dual capacity, absent a showing that the estate suffered damages. The probate court denied petitioners' claim to surcharge Palis.

Thereafter, Palis filed a petition to recover professional fees for himself and his lawyer in the amount of \$51,420 and \$11,100, respectively. Petitioners objected to the petition, claiming that Palis sought reimbursement for attorney fees and costs for work which did not benefit the Trust by increasing or preserving its assets. Further, petitioners objected because the probate court's opinion did not address payment of attorney fees. Similarly, petitioners objected to an award of fiduciary fees to Palis because the probate court's opinion did not allow for an annual accounting and did not address the sum of fiduciary fees or the objections to those fees.

The probate court issued a supplemental opinion in June of 1997. According to the probate court, the petitioners' objection to fees was closely identified with their objection to the account and to their petition for surcharge. The probate court determined that Palis and his attorney substantially complied with MCR 8.303 by submission of an itemized statement of services rendered. The probate court stated:

The time and service of the trustee were well documented and as indicated, scrutinized on a consistent basis. Although there were disputes as to management decisions and the timeliness of certain activities, the court made no findings that the trustee failed to meet his obligations in a timely manner. The beneficiaries, as indicated, had disputed the trustee's fidelity and loyalty which allegations were adjudicated and the resulting Opinion of December 16, 1996 issued.

* * *

As to the attorney fees, this unique proceeding presented a number of issues requiring a high degree of skill in advising the fiduciary. Counsel for the fiduciary, as well as all counsel representing the beneficiaries, were timely and well prepared in dealing with the issues presented to the court. . . . The attorney is charging the estate at the agreed upon rate of One Hundred and 00/100 (\$100) per hour, which is well within the hourly rate charged for work for similar legal services within the community. . . .

As to the attorney's work benefiting the estate, or benefiting the trustee individually -- that issue had been resolved in favor of the trustee and his attorney per the Opinion dated December 16, 1996. The ongoing business enterprise, the trust activity, the dealing with the trust beneficiaries required an ongoing and consistent representation by the attorney, which although the proceeding became lengthy, disputed matters were brought before the court in a timely fashion.

After reviewing the statement for services rendered and the submission offered to refute it, the court concludes that 10% of the fiduciary fee is not warranted having accepted the objector's argument that some of the fiduciary's efforts did not require a

professional fiduciary but the tasks could be performed by an assistant or layman such as in the area of paying ordinary bills or expenses.

The probate court issued an order consistent with its supplemental opinion, awarding attorney fees and fiduciary fees to Palis.

II. Standard Of Review

A. Self-Dealing And Conflicts Of Interest

This Court reviews a probate court's findings of fact to determine whether they are clearly erroneous. *In re Green Charitable Trust*, 172 Mich App 298, 311; 431 NW2d 492 (1988). "Findings are clearly erroneous when this Court is left with the definite and firm conviction that a mistake has been made." *Id.* Because petitioners requested that the probate court surcharge Palis as trustee of the Trust based on his alleged breach of his fiduciary duties to the Trust, this issue is preserved for appellate review.

B. Fiduciary Fees

"The weight to be given any factor and the determination of reasonable compensation is within the probate court's discretion." *Comerica Bank v City of Adrian*, 179 Mich App 712, 724; 446 NW2d 553 (1989). Because petitioners objected to Palis's request for fiduciary and attorney's fees, the issue is preserved for appellate review.

III. Self-Dealing And Conflicts Of Interest

Petitioners argue that the probate court erred in denying their claim to surcharge Palis in light of Palis's self-dealing and his conflicts of interest. We disagree.

Generally, the duties imposed on the trustee are determined by consideration of the trust, the relevant probate statutes and the relevant case law. *Green Trust, supra* at 312. The question whether a trustee has breached his fiduciary duties, subjecting him to liability, is determined based on the facts of the given case. *Id.* The trustee is expected to act as "a prudent man dealing with the property of another, and if the trustee has special skills or is named trustee on the basis of representations of special skills or expertise, he is under a duty to use those skills." *Id.* at 312-313, quoting MCL 700.813; MSA 27.5813. This duty includes acting with care, diligence, integrity, fidelity and sound business judgment. *Id.* at 313. Courts have also imposed on trustees the fiduciary duties of honesty, loyalty, restraint from self-interest and good faith. *Id.*

Here, Palis was named as successor trustee under § 13 of the Second Amendment to the Trust Agreement. Section 5(c) of the Trust Agreement provided that the trustee would have the power "to retain the property in the trust fund and any property added to the trust fund, without liability for any decrease in value, and without being restricted in said retention to property authorized by the laws of the State of Michigan or of any other jurisdiction for trust investments." Granting trustees discretionary or broad powers does not mean that the trustee's powers are limitless. *Id.* at 313. The trustee's actions

will be reviewed for an abuse of discretion. *Id.* The trustee must exercise his discretion honestly and in good faith. *Id.* Bad faith has been defined as “arbitrary, reckless, indifferent, or intentional disregard of the interests of the person owed a duty.” *Id.* at 315 (citation omitted). Bad faith is not a specific act, but defines the character or quality of a party’s actions. *Id.* Whether bad faith exists depends on the facts of an individual case. *Id.*

Petitioners argue that Palis acted in bad faith and breached his fiduciary duties to the Trust because his personal interests were directly in conflict with the Trust’s interests. Petitioners assert that Palis was too involved with Applied Industries, which owed the Trust money through a promissory note, to act in the best interest of the Trust.

Admittedly, Palis owned the building which Applied rented, leased machinery to Applied and provided accounting services to Applied for a fee. However, the record indicates that Palis made no profit on these transactions. In fact, Applied’s rental fee for the building and equipment were at or below fair market value. Palis did not charge Applied for all his accounting services. Further, Reid, prior to his death, was aware of and consented to Palis’s rental agreements. The record indicates that Applied benefited from renting a building partially owned by Palis. Indeed, Palis and his partner allowed Applied to remain in their building for over a year without paying rent. The record reflects Palis was not treated more favorably than any other potential creditor. In fact, Applied used its relationship with Palis to obtain favorable deals. Standing alone, the fact that Palis worked in a dual capacity does not subject him to liability. See *Mintener v Michigan National Bank*, 117 Mich App 633, 641; 324 NW2d 110 (1982).

Petitioners also assert that Palis’s ownership interest in Applied and his position on its board motivated him to place his personal interests above the interests of the Trust. According to petitioners, Palis never attempted to realize any value on the Trust’s \$555,000 promissory note issued by Applied because of his personal financial stake in Applied. Further, petitioners argue that Palis’s belief that Applied was going to receive a lucrative contract from GM and BMW was merely an excuse to cover his own self-interest.

Prior to his death, Reid never requested interest payments on his promissory note from Applied. Had Palis demanded interest payments on the note, or repayment of the note itself, Applied would have gone bankrupt. If Applied had gone bankrupt, petitioners would not have been secured creditors because Reid failed to renew his secured interest in the promissory note. In addition, Palis was unaware that his promissory note and the Trust’s promissory note were no longer secured debts. Moreover, Palis believed that there was a good chance that Applied would become profitable. Because there was a reasonable chance that Applied could have recovered from its economic downturn, Palis attempted to maintain Applied’s operations. For the small amount of money that the Trust would have realized from the closing of Applied, compared to the potential value of the Trust’s assets if Applied would have been awarded the GM/BMW contract, we believe that Palis made a reasonable business decision to continue operations.

However, petitioners assert that the Trust was damaged in two ways. First, petitioners contend that they were entitled to monetary damages for the difference between the valuation of the Trust’s

Applied assets on the 706 estate tax form and the amount of money eventually received by the Trust after the liquidation of Applied. Second, petitioners argued that the Trust is entitled to recover damages for paying federal estate taxes on worthless assets related to Applied.

The record reflects that Palis retained the help of an expert in the area of probate matters to assist him in filing the 706 tax form. The estimate regarding the value of the assets was based on numerous factors, including the fact that Applied had realized a profit in 1990 and the possibility of winning the GM/BMW contract. Palis's actions were not arbitrary or reckless. Because Palis took the proper steps to obtain a reasonable estimate of the worth of the Trust's assets at the time of Reid's death, we do not believe that petitioners were entitled to surcharge Palis for the Trust's losses.¹

Petitioners argue that the record is undeniably clear that Palis acted in bad faith with regard to Applied's assets. However, petitioners offer nothing more than mere allegations. Because there is no evidence on the record that Palis's decisions were grossly negligent or made in bad faith, we believe that the probate court did not err in denying petitioners' surcharge claim.

IV. Fiduciary Fees

Petitioners contend that the probate court erred in awarding Palis fiduciary fees when his claimed services did not benefit the Trust or its beneficiaries. We disagree. "[A] trustee is entitled to just and reasonable compensation for services rendered." *Comerica Bank, supra* at 723. The Revised Probate Code provides:

A fiduciary shall be allowed the amount of his or her reasonable expenses incurred in the administration of the estate and shall also have such compensation for his or her services, both ordinary and extraordinary as the court in which the fiduciary's accounts are settled deems to be just and reasonable. . . . [MCL 700.541; MSA 27.5541.]

Unless the trustee's fees are provided for in a written instrument, the trustee must file a written description of services performed or a statement otherwise indicating the basis of a claim for compensation. *Comerica Bank, supra* at 723-724; MCL 700.541; MSA 27.5541; see also MCL 5.722. Therefore, the court determines the reasonable value of the services provided by the trustee. *Comerica Bank, supra* at 724. While time spent is an indicator of value, it may be a poor indicator in some circumstances. *Id.* When determining which factors are to be given weight, the probate court must consider the circumstances of the case. *Id.* The claimant bears the burden of proof that the services rendered were necessary and that the charges were reasonable. *Id.*

Here, the probate court determined that Palis was entitled to compensation for his services rendered to the Trust. Palis testified that his fees were in accordance with the Trust Agreement. Palis submitted detailed billings and asked the probate court to adopt his accounting. Furthermore, Palis testified that his accounting of services rendered to the Trust was true and accurate. Petitioners failed to present any evidence to the contrary. In fact, petitioners' objection to the award of fiduciary fees did not relate to the rate per hour or the details provided by Palis. Instead, petitioners objected to the

award of fiduciary fees because Palis's services were not incurred in pursuit of the best interests of the Trust.

Because we do not believe that the evidence on the record reflects any wrong-doing on the part of Palis, as trustee of the Trust, petitioners' objections to Palis's request for fees was properly denied by the probate court. It is clear that the probate court examined the record, reviewed Palis's itemized request for fiduciary fees and considered petitioners' objections when it decided to award Palis his requested fiduciary fees minus 10%. Therefore, the probate court did not abuse its discretion in awarding Palis fiduciary fees.

Affirmed.

/s/ William C. Whitbeck

/s/ Mark J. Cavanagh

/s/ Richard Allen Griffin

¹ Even if we were to believe that Palis's business decisions were unsound, the Trust Agreement effectively limited his liability. Section 12(o) of the Trust Agreement provides:

No Trustee acting hereunder shall be held liable to any trust or beneficiary thereunder in respect of any loss, cost, damage or expense sustained through any error of judgment or in any other manner except as a result of such Trustee's bad faith or gross negligence.

A trustee's potential liability may be limited by the terms of the trust instrument. *In re Green Trust*, *supra* at 313-314. Generally, an exculpatory clause does not reduce or enlarge the standard of care required of the trustee in administering the trust, but acts to relieve the trustee of personal liability under the stated circumstances. *Id.* at 314. Exculpatory clauses generally do not mean that the trustee is not accountable to anyone for the trustee's actions. *Id.*