IN THE COURT OF APPEALS OF IOWA

No. 9-263 / 07-2122
Filed July 2, 2009

IN THE MATTER OF THE JOHN F. MCKERNAN, JR. TRUST

JUDITH ANN MCKERNAN and BRIAN MCKERNAN,
Trustees-Appellees/Cross-Appellants,

vs.

MONTGOMERY G. MCKERNAN,
Beneficiary-Appellant/Cross-Appellee.

Appeal from the Iowa District Court for Story County, Dale E. Ruigh, Judge.

Montgomery McKernan appeals from the district court ruling denying his petition to remove the trustees of the John F. McKernan, Jr. Trust. **AFFIRMED.**

Montgomery McKernan, Ames, appellant pro se.

Theodore F. Sporer and Meghan S. Hanson of Sporer & Flanagan, P.C., Des Moines for appellant/cross-appellee.

James L. Spellman of Law Offices of James Spellman, Des Moines, for appellees/cross-appellants.

Heard by Vaitheswaran, P.J., and Potterfield and Doyle, JJ.

VAITHESWARAN, P.J.

We must decide (1) whether the district court acted equitably in declaring all, rather than some, of John F. McKernan Jr.'s children the beneficiaries of a trust created by him, (2) whether the trustees should have been removed, and (3) whether the district court appropriately denied the trustees' claim for compensation.

I. Background Facts and Proceedings

McKernan, the father of seventeen children, executed a trust agreement the day before he died. The agreement named his wife, Judith McKernan, and son, Gregory McKernan, the trustees. Another son, Brian McKernan, was written in as "Manager Trustee."

Article I of the trust agreement states in pertinent part:

> The trustor's minor children now living with him and his wife are Devon C. McKernan, Montgomery G. McKernan, Jennifer K. McKernan and Katrina VanKleeck McKernan. All references hereto to the trustor's child or children shall refer only to the above-named children.

Notwithstanding this seemingly clear instruction, another portion of the trust agreement referred to "the children named in Article III." That article listed only Gregory and Brian. A third article of the agreement provided for distribution of the residuary trust to "each then living child of the trustor," as follows:

> At the death of the trustor's wife, the trustees shall divide the RESIDUARY TRUST, together with property from any other source, into equal shares so as to provide one share for each then living child of the trustor and one share for the then living descendents collectively of each deceased child of the trustor.

An attachment to the trust document titled "Schedule B – Beneficiaries and Children" listed all seventeen children of the trustor.

The four children named in Article I of the trust agreement petitioned for removal of the trustees and the naming of a replacement trustee. They alleged that the trustees had not made distributions. They sought a complete accounting of all trust assets and expenses, removal of Judith and Brian as trustees[1] for "multiple, serious and ongoing breaches of their fiduciary duties," the appointment of Montgomery as the successor trustee, and an award of costs and attorney fees against Judith and Brian. Judith and Brian filed an answer admitting that no distributions were made, but stating the children's financial needs were met and all the children were currently self-supporting. They counterclaimed for a determination of fees and compensation "for [Brian's] personal improvements to the Trust properties and for his capital contributions to the Trust." Finally, the defendants asked the court to declare all seventeen of John's children beneficiaries of the trust.

At trial, the district court was informed that two of the petitioners, Jennifer and Katrina, did not wish to remain petitioners. Accordingly, trial proceeded with only Devon and Montgomery as petitioners.

Following trial, the district court concluded that John intended his entire family to benefit from the trust. The court declined to remove Brian and Judith as trustees and declined to compensate Brian as he requested.

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[1] Gregory resigned before this litigation.

Montgomery filed a notice of appeal.[2] The parties state that our review is de novo, as all aspects of the case were tried in equity. *Garland v. Brandstad*, 648 N.W.2d 65, 69 (Iowa 2002).

II. Beneficiaries of Trust

As noted, the district court concluded that all seventeen children of John were residual beneficiaries of the trust. Montgomery argues that the court's conclusion is contrary to the plain language of the trust agreement. He asserts that the court erroneously relied on the list of seventeen children marked as Schedule B, even though that list was not expressly incorporated into the trust agreement as required by "the doctrine of incorporation." *See Longfellow v. Saylor*, 737 N.W.2d 148, 154 (2007) ("The doctrine of incorporation requires the contract to make a clear and specific reference to an extrinsic document to incorporate the document into the contract."). We are not persuaded by this argument.

It is well established that courts may look beyond the words used in the trust agreement to ascertain a trustor's intent:

> The polestar of our analysis is the rule that the testator's (or, in this case, the settlor's) intent must prevail. That intent is to be determined from the language of the instrument, the scheme of distribution, and the facts and circumstances surrounding the document's execution.

In re Trust of Killian, 459 N.W.2d 497, 499 (Iowa 1990). It is also clear that "[t]echnical rules of construction are resorted to only if the settlor's intent remains uncertain after that inquiry." *First Nat'l Bank of Dubuque v. Mackey*, 338 N.W.2d 361, 363 (Iowa 1983). Based on this precedent, the district court was fully

[2] It appears that Devon is not a party to the appeal.

empowered to consider Schedule B and accompanying evidence of the trustor's intent, whether or not it was expressly incorporated by reference into the trust agreement.

That schedule, together with the testimony of key witnesses, clarifies that the trustor intended to benefit all his children, not just the four children listed in Article I. Brian testified that his father "wanted to make sure that he treated each one of his kids fairly." He said Schedule B was attached to the trust agreement because his father indicated he wanted all seventeen of the children to share in the distribution of the trust. Judith similarly testified that Schedule B was prepared because John "wanted to make sure that . . . all of his children were part of the trust."

Some of John's other children made similar statements. Gregory testified that he understood his father's intent was a distribution that was "[e]qual to all of his surviving children." He testified that a limited distribution to the four children listed in Article I would have been "wholly unlike anything my dad ever did in his life." Pamela testified that her father wanted his assets to be distributed among the seventeen beneficiaries. Cynthia testified that John wanted all the children to be a part of the "McKernan heritage." She believed all seventeen children were to benefit from the trust. Kimberly testified that her father wished to have all seventeen children benefit from the trust.

Based on this record, we concur with the district court's declaration of all seventeen children as beneficiaries of the trust.

***III.* Removal of Trustees.**

Montgomery contends Brian and Judith should have been removed as trustees because they (1) failed to disburse funds, (2) commingled their assets with trust assets, and (3) refused to provide the beneficiaries with accurate accountings. The standard for removal of trustees is the best interests of the operation of the trust. *Schildberg v. Schildberg*, 461 N.W.2d 186, 191 (Iowa 1990).

On the first point, the trust agreement vested the trustees with discretion to disburse funds for the minor children's maintenance, and Brian testified the trust initially lacked assets to make disbursements. Despite the absence of trust funds, family members, including Brian and Judith, cared for the minor children and provided for their needs when necessary.

Turning to Brian's conceded commingling of trust assets with personal funds, we conclude this practice was a recipe for fraud. However, we agree with the district court that there was no showing Brian and Judith "benefited improperly from those operations." *See id.* ("There is no evidence to indicate that the omission to report resulted from a motive on the part of Dennis to take advantage of the beneficiaries."). The trust increased in value with Brian and Judith at the helm, rising from bankruptcy to a positive net worth of $329,000.

As for Brian's failure to provide an accounting, there is no question this was a breach of the trust agreement. However, the breach was somewhat mitigated by Brian's willingness to allow his siblings access to the books and records of the trust. *See id.* (finding no evidence that the effectiveness of the trust was impaired by the technical violation of the reporting requirement).

For these reasons, we affirm the district court's refusal to remove the trustees.

IV. Trustee Compensation.

Brian sought compensation for his services as trustee. The district court stated it "ha[d] no competent factual basis upon which to base a determination of reasonable compensation" and said, "In any event, Brian testified that, if he was allowed to continue living on the farm, he would not pursue his request for compensation." Brian cross-appealed from this ruling.

On our de novo review, we find support for the district court's findings and we concur with the court's decision to deny Brian compensation.

AFFIRMED.