Title

When virtual representation is not an option in trust-reformation litigation

Text

In an external contract-based or tort-based dispute between the trustee and a third party to the trust relationship, the beneficiaries are generally not necessary parties. But all beneficiaries (of an irrev. trust) *whose equitable property rights might be compromised by the litigation* must be given an opportunity to participate in an internal trust dispute, even any beneficiaries yet to come into existence, such as the settlor's future descendants (issue) who are designated to take the remainder in corpus ("future benes"). An action for instructions or declaratory judgment qualifies as such a dispute, provided equitable property rights are at stake. So also an action to reform the trust. The court's ultimate determination would not be binding on future benes whose equitable property have been compromised by the determination unless a guardian ad litem had advocated for their equitable property rights or they had been "virtually represented."

One codification of the doctrine of virtual representation is Uniform Trust Code's Section 304: "Unless otherwise represented, a minor, incapacitated or unborn individual, or a person whose identity or location is unknown and not reasonably ascertainable, may be represented by and bound by another having a substantially identical interest with respect to the particular question or dispute, but only to the extent there is no conflict of interest between the representative and the person represented." But the UTC may not pre-empt the U.S. Constitution. Thus, virtual representation may not be a vehicle for end-running the Due Process Clause. *See* Roth v. Jelley, 45 Cal. App. 5th 655, 259 (2020). The judiciary being a state actor, even an equitable trust-reformation order that would erode the contingent equitable property rights of future benes is subject to due process constraints. For examples of conflicts of interest that foreclose virtual representation, see §8.14 of *Loring and Rounds: A Trustee's Handbook* (2025), excerpted in appendix below.

Terteling v. Terteling, 2024 WL 4644904, Idaho Sup. Ct. (11/1/2024), involved an irrev. trust the terms of which restricted a class of future benes to co-trustees' male descendants. Petitioners sought judicial reformation to expand class to include female descendants. Expansion would partially divest via dilution male descendants' pre-existing contingent equitable property rights. A presumptive male class-member objected. No GAL was appointed to represent the other future benes, the court presumably being comfortable that objectant's participation was adequate "representation" of their property rights. The court's finding clear and convincing extrinsic evidence of mistake replaced restrictive language with gender-neutral language.

But was it prudent for the court to forego appointing a GAL to advocate for the property rights of the other male future benes? What if objectant had contractually agreed mid-course to switch sides? Or simply abandoned the litigation? Or died mid-course? A GAL would then have to have been appointed mid-course and duly served with the reformation complaint to ensure that any judicial determination adverse to the male future benes would be constitutional and thus final and binding as to them. Back to square one.

As an aside, while the GAL would owe no fiduciary duties to the yet-to-exist male future benes, he/she at least would have owed agency-based fiduciary duties to the court. See my 11/28/2024 JDSUPRA posting, accessible below or by clicking on to https://www.jdsupra.com/legalnews/when-the-guardian-ad-litem-representing-5208844/. As one

cannot enter into an agency relationship with the non-existent, neither objectant nor his counsel had truly "represented" the yet-to-exist male future benes. The objectant himself had owed fiduciary duties to no one. The equity court thus had had an "administrative" duty to step into the breach, to act *sua sponte* in vindication of whatever contingent equitable property rights that had accrued *at time of irrevocable entrustment* to the unrepresented male future benes, the institution of the trust being equity's ward as well as its invention.

Appendix

§8.14 When a Guardian ad Litem (or Special Representative) Is Needed: Virtual Representation Issues [from *Loring and Rounds: A Trustee's Handbook* (2025)].

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The conflict-of-interest disqualification. Assume a trust under which members of *X* class take a vested remainder interest subject to divestment upon the fulfillment of a condition subsequent.[31] If the condition is fulfilled, the property passes outright and free of trust to the then-living members of *Y* class, *Y* class being the issue of the members of *X* class. If there was litigation over whether the trustee had invested the principal prudently, the *X* class could represent the members of *Y* class in a jurisdiction that recognized the doctrine of virtual representation. Why? Because each class would have an identical interest in the subject of the litigation—namely, the well-being of the principal account.[32] On the other hand, if the litigation was over whether or not the condition subsequent had been fulfilled, the members of *X* class could not represent the members of *Y* class because the interests of each class in the litigation would be in conflict: It is in the interests of the members of *X* class that the status quo be preserved, i.e., that the condition subsequent had not been fulfilled; it is in the interests of the members of *Y* class that the members of *X* class be divested of their equitable interests, i.e., that the condition had been fulfilled.[33]

Or take a trust with the following provisions: *A* to *B* for *C* for life, then to John Jones outright and free of trust if he is living at *C*'s death; but if John Jones is not then living, to his then-living issue from his first marriage.[34] Absent special facts, it is likely that either *C* or John Jones could represent the other beneficiaries in an action to remove the trustee, that is *B,* and appoint a suitable successor to *B.*[35]

Now let us assume that *C* wishes a distribution of principal, but the governing instrument is silent on the matter. Under the doctrine of "virtual representation," the assent of John Jones to the distribution is probably not binding on the issue. This is because a distribution of principal is a form of partial termination. As a general rule, a presumptive remainderman may not represent alternative remaindermen when it comes

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[31]*See, e.g.*, Robertson v. Hert's Adm'rs, 312 Ky. 405, 227 S.W.2d 899 (1950) (involving virtual representation of a class of remaindermen who would take the equitable interest should another class be divested of its interest). *See generally* §8.30 of this handbook (the difference between a vested equitable remainder subject to divestment and a vested (transmissible) contingent equitable remainder).

[32]*See generally* UTC §304 cmt. (suggesting that whether identity of interest is present may depend upon the nature and subject of the litigation).

[33]For actual decisions in which the virtual representation doctrine has been applied, *see* Bogert §871, n. 42.

[34]*See* §8.30 of this handbook (the difference between a vested equitable remainder subject to divestment and a vested (transmissible) contingent equitable remainder).

[35]*See, e.g.*, Davis v. U.S. Bank Nat'l Ass'n, 243 S.W.3d 425 (Mo. Ct. App. 2007).

to trust termination issues.[36] Insuring against John Jones predeceasing *C* might be a practical way around the impasse.[37] Another option might be for John Jones to agree to indemnify the trustee for any liability occasioned by the trustee's making principal distributions to *C*.[38] "In short, where the rights of infants and incompetents are concerned, virtual representation never assures the same finality in decree as does representation by a guardian ad litem."[39] Also, the particular facts and circumstances alone can give rise to a conflict of interests: if *C*, for example, is John Jones' second wife while the issue owe their very existence to his first marriage.[40] It is by no means a given that the issue would have assented to the distribution of principal to someone not their ancestor.

In one case, a victim of the terrorist attack on the World Trade Center on September 11, 2001, was survived by his wife and two children, one of whom was a minor. The core of his estate plan was two trusts, a standard combination of credit shelter trust and marital deduction trust.[41] The two children were remainder beneficiaries under each trust. There were three cotrustees: the widow and the victim's two brothers. The two brothers took the position that the credit shelter allocation was governed by the Victims of Terrorism Tax Relief Act of 2001, and that the Act effectively raised the amount that was allocable to the credit shelter trust beyond the exclusion amount of $675,000 applicable in 2001 to the point where there would be nothing allocable to the marital deduction trust.

The widow and her adult son took the position that the Act was inapplicable. The son's position was against his own economic interests: "After all, if the marital deduction trust is funded by limiting the credit shelter trust to the exclusion amount of $675,000, then the remainder interest of the two children in the marital deduction trust may be reduced by virtue of the taxability of the remainder of the marital deduction trust, the standard 'five and five' limited right to principal of the marital deduction trust of the mother, and the standard of living component of the marital deduction trust, not to mention the tax-free quality of the remainder of the credit shelter trust."[42]

Could the brother virtually represent the sister? The New York courts have traditionally looked to three criteria when asked to resolve such issues:

- Similarity of economic interest between the representor and the representee;
- The absence of any conflict of interest between them; and

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[36]UTC §304 cmt. *See generally* §8.2.2.1 of this handbook (trust terminations by consent); 5 Scott & Ascher §34.4 (When Some of the Beneficiaries Do Not or Cannot Give Binding Consent).

[37]*See* Rest. (Third) of Trusts, Reporter's Notes on §65 cmts. b, c.

[38]Rest. (Third) of Trusts, Reporter's Notes on §65 cmts. b, c.

[39]*In re* Est. of Putignano, 82 Misc. 2d 389, 395, 368 N.Y.S.2d 420, 428 (Sur. Ct. 1975).

[40]For a case in which such "external factual considerations" foreclosed virtual representation of minor children, *see* Mennen v. Wilmington Tr. Co., No. 8432-ML, 2015 Del. Ch. LEXIS 120, at *76–77 (Del. Ch. Apr. 24, 2015): "The evidence at trial removed any doubt that, with respect to the transactions challenged in this section, John … [, a beneficiary of the trust,]… has a material conflict with his … [minor] children because (1) he placed nearly complete emphasis on the present income of the Trust, without any apparent regard for the capital growth or long-term stability of the Trust, and (2) he was beholden to Jeff … [the individual cotrustee]… to the point that John could not himself take action to remedy Jeff's bad faith conduct." *See generally* UTC §304 cmt.; 5 Scott & Ascher §34.4.

[41]*See generally* §8.9 of this handbook (why more than one trust: the estate and generation-skipping tax).

[42]*In re* Est. of Dickey, 761 N.Y.S.2d 473, 474 (Sur. Ct. 2003). *See generally* §8.9 of this handbook (why more than one trust: the estate and generation-skipping tax) and §9.18 of this handbook (the *Crummey* trust) (discussing in part the "5 and 5" limitation).

- The adequacy of the representation by the representor of the representee.[43]

While there may have been technical compliance with all three criteria in this case, the court, "mindful of its obligation to guard the finality of its decrees" and to be "vigilant in the protection of the interests of persons suffering from a disability," exercised its discretionary authority to order the appointment of a guardian ad litem to represent the minor daughter. While the adult son's position against his own economic interests may have been "reasonable and even laudable," the court was simply not comfortable allowing him to speak for his minor sister, his position being adverse to his sister's economic interests as well.[44] The court noted that it was not convinced that even an independent guardian ad litem acting on behalf of the minor daughter could or should adopt the widow's position that the marital deduction trust was entitled to an allocation at the expense of the credit shelter trust.

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[43]*In re* Est. of Holland, 84 Misc. 2d 922, 377 N.Y.S.2d 854 (Sur. Ct. 1974); *In re* Est. of Putignano, 82 Misc. 2d 389, 368 N.Y.S.2d 420 (Sur. Ct. 1975). *Cf.* 5 Scott & Ascher §34.4 (noting that under New York law the settlor may revoke the trust upon the written consent of all persons "beneficially interested").

[44]*See generally* 5 Scott & Ascher §34.4 (Absence of a Conflict of Interest Is Critical When It Comes to Virtual Representation).