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THE SPOTLIGHT

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WEALTH PLANNING, ADMINISTRATION,
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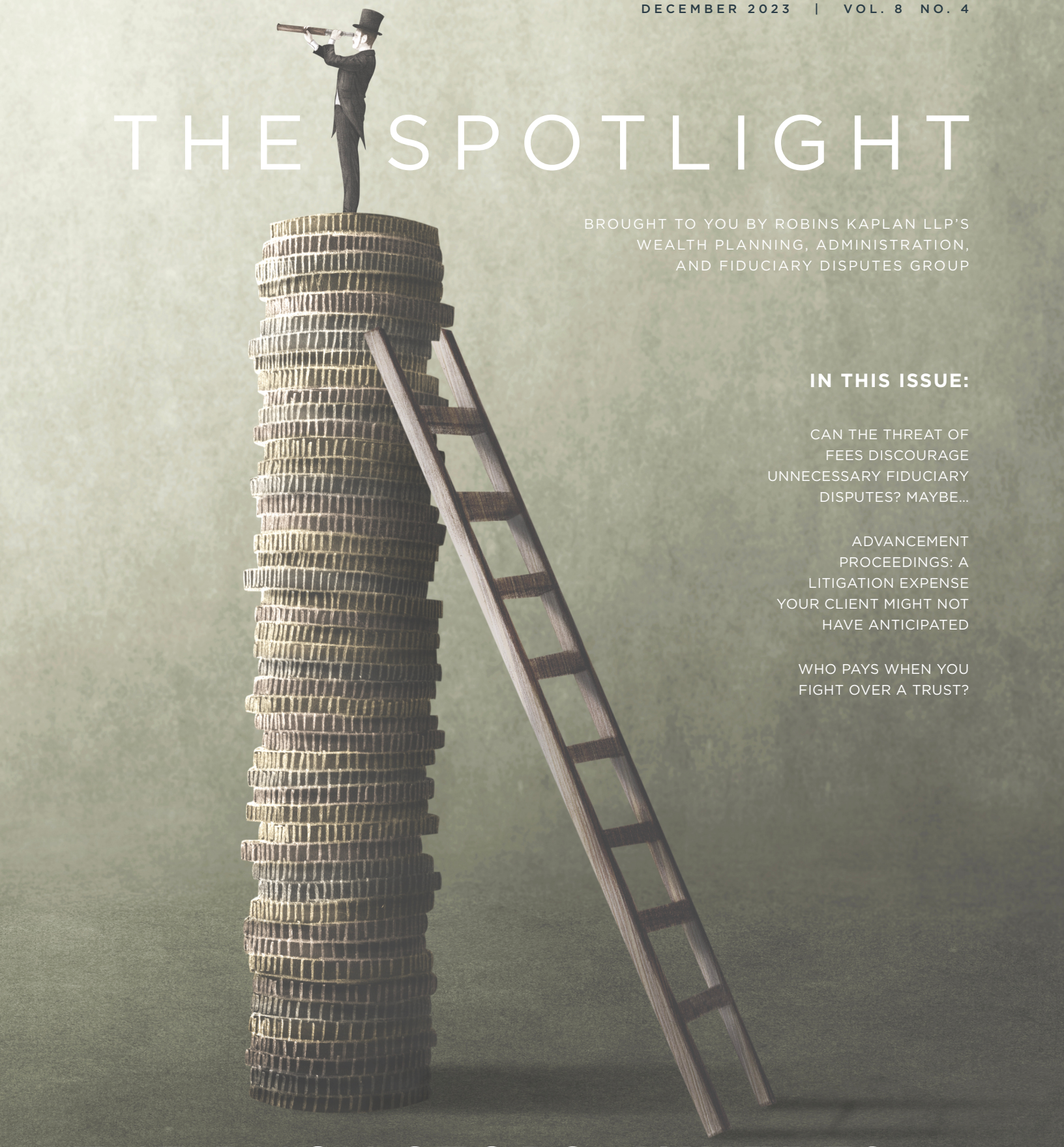

IN THIS ISSUE:

THE BUCK STOPS...**WHERE?**

ATTORNEY FEE ISSUES IN FIDUCIARY LITIGATION

WELCOME TO THE SPOTLIGHT

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The Spotlight strives to provide a forum to discuss the latest news and compelling issues impacting fiduciaries and those to whom fiduciaries owe duties. Whether you are an officer, director, trustee, beneficiary, trust officer, attorney, financial advisor, or anyone impacted by the law governing fiduciaries, we hope that you will find this newsletter interesting, informative, and perhaps at times even a bit entertaining.

Fiduciary disputes come in many varieties, but they share some consistent themes that involve the erosion of trust, high emotion, and opportunities—sometimes missed—for creative approaches to avoid or resolve litigation. As practitioners and teachers of fiduciary law, our attorneys have built a reputation for excellence in meeting the needs of individuals and organizations facing complex fiduciary issues, starting with the transactional and estate planning work that can mitigate risk from the beginning. We counsel individuals and business owners in a broad range of fiduciary issues, from estate planning and business succession, to dispute resolution and litigation when unavoidable.

Is there a topic affecting your practice that you would like us to discuss in an upcoming issue of The Spotlight? Let us know at all_marketing@robinskaplan.com.

– Denise S. Rahne and Steven K. Orloff

CAN THE THREAT OF FEES DISCOURAGE UNNECESSARY FIDUCIARY DISPUTES? **MAYBE...**

BY MANLEEN SINGH AND DENISE RAHNE

The early stages of partner and shareholder relationships are about hope and promise, not discord and dispute. Yet, the earliest stage—and during the drafting of the partner or shareholder agreement—offer real opportunities to address and potentially discourage disputes.

One often-utilized approach comes in the form of fee- and cost-shifting provisions. At the highest level, such provisions are designed to force a potential litigant to thoroughly assess the likelihood of success prior to starting a legal dispute. But, as the case with most legal tools, the level of efficacy is somewhat nuanced.

A TYPICAL FEE-SHIFTING PROVISION

Fee-shifting provisions will generally incorporate a range of potential legal proceedings and allow the prevailing party to recover reasonable fees and costs if such a proceeding is initiated. A common and not necessarily recommended example follows:

Fee Shifting: Should any legal action, arbitration, or proceeding be brought to enforce or interpret any provision of this Agreement, the prevailing party shall be entitled to recover reasonable attorney fees, court costs, and other expenses incurred in connection with such action, in addition to any other relief to which the prevailing party may be entitled.

Typically provisions like this are boilerplate and passed along, cut-and-pasted, without much thought or reflection. Yet, even in those cases, the provisions can provide some benefit, although tailoring them to individual circumstances can improve their relative value.

THE POTENTIAL BENEFIT OF FEE-SHIFTING PROVISIONS

Attorney fee-shifting provisions telegraph the risks and costs associated with a legal dispute. Consequently, such provisions can discourage the most frivolous litigation because the parties to the agreement become motivated to engage in a meaningful risk assessment that includes the financial implications of the dispute if the matter is litigated to a final resolution. Such assessments provide a level of rationality in situations that are often highly emotional and driven by personal animosity.

DRAFTING TIP: Include some language that calls out the risks to the parties. For example, fee-shifting provisions should reference legal costs incurred from mediation, arbitration, litigation, and appeals until a final, non-appealable judgment is reached. The costs identified in this provision should also include, without limitation, attorney fees, expert fees, and court costs. These lists of examples declare what is at stake when a party wants to go to court.

DRAFTING TIP

Most jurisdictions imply a covenant of good faith and fair dealing in every contract, which requires all contracting parties to act reasonable with one another. As a reminder of this obligation, fee-shifting provisions should include clauses that require parties to act reasonably when prosecuting claims against one another and incur only those legal fees and expenses that are proportional to the needs of the case. A reasonableness standard also increases the odds of courts enforcing fee-shifting provisions.

Even when litigation is initiated, these provisions can have a "reasonableness influence" in that they can encourage parties to act more reasonable within the litigation to increase the likelihood that parties can recover their fees should they prevail and protect against losses should they not. When such provisions are most effective, they can lead to more efficient legal strategy and disincentivize petty legal tactics.

Fee-shifting provisions can also encourage settlement at many stages of litigation. Early phases of the proceedings present the parties with the opportunity to preserve unspent resources and control the outcome. In later phases, each party needs to assess the reality that the fees and costs incurred over the entire litigation could become their responsibility. Such uncertainty can encourage a pragmatic rationality that leads to the parties taking the outcome into their own hands and working together to minimize the looming risk that could become any respective party's ultimate responsibility.

THE MAYBE

Some aspects of fee-shifting provisions are more nuanced. Most notably, many laud fee-shifting provisions for accomplishing a sort of "leveling the playing field" and potentially balancing financial burdens where a party with a viable claim is under-resourced. That said, a party can only realize this benefit by seeing a matter through to the end, prevailing, and then convincing a court that their fees and costs were reasonable. In addition, in some cases, the party with more financial resources might use fee shifting as a strategic advantage, pressuring the other party to settle despite the merits of the case.

Common aspects of fee-shifting provisions can also implicate their efficacy. For example, the deceptively simple question of what it means to be a prevailing party can present myriad complications. If you prevailed on three of your five claims, are you wholly a prevailing party? If you prevailed on all your claims, but your damages were de minimis, are you wholly a prevailing party? If you were found to have breached a duty, but there is no damage, who is the prevailing party?

And then there is the related question of what constitutes reasonable fees and costs and whether they were incurred in connection with the action on which one has prevailed. Practically speaking, for the small percentage of cases tried to a verdict, determination of fees and costs presents an additional and potentially onerous stage of the litigation with a range of attendant risks. Such risks include limited fee recovery and a round of expensive appellate proceedings associated with the fee award, among other things.

CONCLUSION

Ultimately, fee-shifting agreements can discourage frivolous litigation, promote a degree of fairness, incentivize settlement, and encourage reasonable behavior during disputes. That said, they are not a panacea, and parties and potential parties should not be overly taken in by their ultimate impact. In addition, depending on the specific circumstances, careful attention to aspects of such provisions can increase the likelihood that they are a net positive for all parties to the agreement should things not turn out the way they had hoped.

MANLEEN SINGH advises businesses of all sizes on all facets of corporate transactional law, including mergers and acquisitions, commercial leasing, and contract drafting and negotiation.

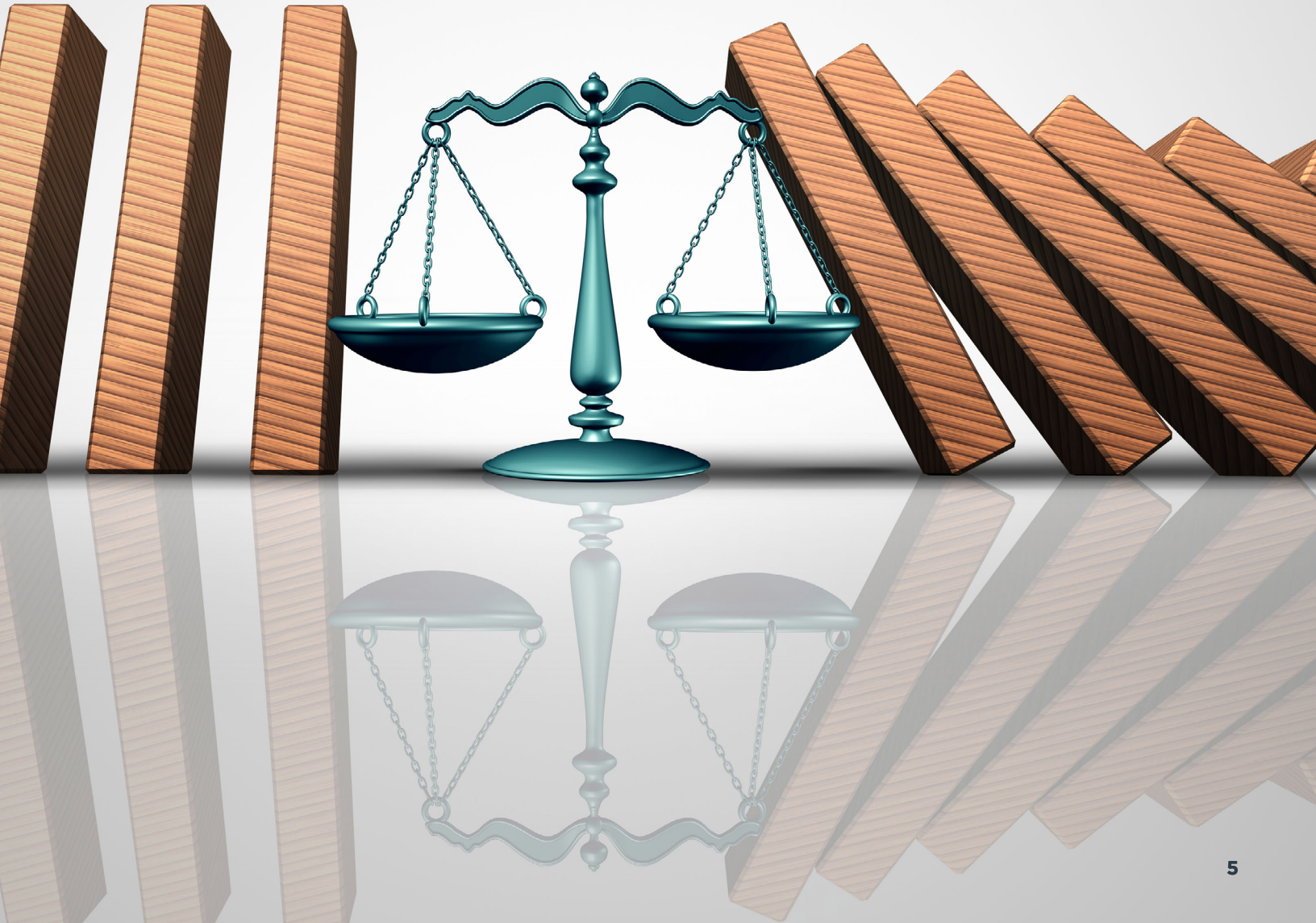
DENISE RAHNE is co-chair of the Wealth Planning, Administration, and Fiduciary Disputes Practice Group. Her practice focuses on disputes involving estates, trusts, fiduciaries, shareholders, and closely-held corporations.

ADVANCEMENT PROCEEDINGS:

A LITIGATION EXPENSE YOUR CLIENT MIGHT NOT HAVE ANTICIPATED

BY ANNE M. LOCKNER

When representing a client, it is helpful when law and logic align in an obvious manner. But alignment of law and logic sometimes appears murky at best, and often directly at odds. An example of this is when you need to explain that your client must pay for the defense of the officer and director it sued for wrongdoing.



A corporation is often obligated under the corporation's bylaws or by contract to advance defense costs, including attorney's fees, when its officer or director is sued in that capacity—even if the corporation is doing the suing. The logic behind the obligation is that corporations would be hard pressed to find qualified individuals to serve as officers and directors if those individuals then faced risks of being sued for acts they took while serving in those capacities. As the Delaware Supreme Court explained in *Stifel Financial Corp. v. Cochran*, the purpose of advancement is to "promote the desirable end that corporate officials will resist what they consider unjustified suits and claims, secure in the knowledge that their reasonable expenses will be borne by the corporation they have served if they are vindicated," and to "encourage capable women and men to serve as corporate directors and officers, secure in the knowledge that the corporation will absorb the costs of defending their honesty and integrity." 809 A.2d 555, 561 (Del. 2002).

And indemnification rights alone are not necessarily sufficient to protect officers and directors if the right to indemnification often cannot be assessed—or accessed—until a litigation matter concludes. In the meantime, a defendant can incur hundreds of thousands, if not millions of dollars in legal fees defending against such claims. Therefore, a corporation agreeing to not only indemnify but provide advancement of defense costs can give its corporate officer or director comfort that those fees will be paid as they are incurred as opposed to waiting years until the matter is resolved and a final right to indemnification is determined.

But what happens when those officers or directors act wrongfully toward the company, and the company decides to sue them? Then the officers and directors make a request for advancement—from the very same party that is suing them. And, generally, the corporation will have to agree to do so—especially if it is a Delaware corporation. Under Delaware law, very rarely does a corporation have a defense to paying advancement. Only if it can show that no causal connection exists between the underlying proceedings and the defendant's official corporate capacity, as defined by the bylaws or contract, can a corporation evade a request for advancement. But that is rarely the case.

For the cases where Delaware corporations refuse advancement, Delaware has established summary proceedings that make it relatively simple to get fees awarded. The Delaware Chancery Court, where such proceedings are brought, will give priority to advancement suits and schedule them for a prompt hearing. And few defenses apply at this stage. If the contract or bylaws provide for advancement, the likelihood of avoiding advancement costs are slim. The only comfort a company takes is that the individual seeking advancement must provide "an undertaking to repay such amount if it shall ultimately be determined

A corporation agreeing to not only indemnify but provide advancement of defense costs can give its corporate officer or director comfort that those fees will be paid as they are incurred as opposed to waiting years until the matter is resolved and a final right to indemnification is determined.

that such person is not entitled to be indemnified by the corporation[.]" 8 Del. C. Section 145(e). But that determination will not be made in the company's favor for months or years, if ever.

Making things more treacherous for the company refusing to pay advancement expenses is the fact that the officer or director can also seek fees for having to bring the claim for advancement, creating an upward spiral of attorneys' fees for the corporation. Therefore, companies rarely dispute the right to advancement in Delaware. The availability of D&O insurance—which generally covers these advancement costs—also helps corporations swallow this bitter pill.

While corporations are hard pressed to dispute the *right* to advancement, they can dispute the *amount* of those advanced expenses—at least to some degree. For instance, if a defendant is represented by counsel who is also representing other defendants who are not entitled to advancement from the corporation, the corporation is only required to advance those fees and expenses that would have been incurred if the corporate officer or director were the sole defendant. If a defense or litigation activity only partially benefits the individual, then counsel must accordingly make a good-faith allocation of those costs and fees. And, of course, if a litigation activity only benefits the other non-entitled defendants, no advancement on those fees is required.

That said, these types of determinations are often hard for a corporation to win at the advancement stage. Under what has become known as the "*Fitracks* Procedures," first set forth in *Danenberg v. Fitracks, Inc*., a senior Delaware counsel for the party seeking advancement prepares a detailed submission, certifying to the correctness of the amount of the advancement request. Senior Delaware counsel for the opposing party may then object to the amounts requested, certifying the detailed reasons why the amounts sought are not advanceable.

But a Delaware court will not engage in a detailed or granular review of "persnickety disputes" over fees at the advancement stage. After all, until it is clear which claims are indemnifiable and for whom, the court can't decide a proper allocation on expenses. Therefore, "fights about details" should be left to the final indemnification proceeding.

In sum, before a corporation sues one of its officers or directors, it should be very confident that it will prevail. Otherwise, not only will the corporation suffer the expense of pursuing its unsuccessful claims, but it will suffer the expense of defending them, too.

ANNE M. LOCKNER is a partner in the firm's business litigation department who handles complex business disputes, including fiduciary disputes that arise among companies and their shareholders, officers, and directors.

WHO PAYS WHEN YOU FIGHT OVER A TRUST?

BY TIM BILLION

Litigation is often expensive. When a client considers filing a lawsuit or must decide how to handle a lawsuit someone else started, one of the most fundamental questions to ask is: Who pays the lawyers?

Under the American Rule, the default rule in litigation is that each party to a case must pay for its own attorneys. In trust litigation, though, the trust may end up paying the legal fees for multiple parties involved in the litigation, ultimately leaving a much smaller pot of money for the beneficiaries than originally anticipated. As a result, a beneficiary might be surprised to find out that the trust is paying to defend a trustee that the beneficiary is suing. Conversely, a trustee may receive distribution requests from a beneficiary even though the beneficiary is suing the trust.

Given the significance of legal fees, how should trustees and beneficiaries plan for legal expenses when dealing with trust litigation?

Look first to the trust document. The settlor of a trust is unlikely to want to burden a trustee with payment of legal expenses incurred in administering the trust (and a potential trustee is very unlikely to accept that role if it risks exposure to paying legal fees). As a predicable result, most trust documents permit a trustee to hire lawyers, and many will also indemnify a trustee for any expenses that do not result from intentional wrongful conduct—even if that conduct is later determined to be a breach of a fiduciary duty.[1] All parties will want to know the extent to which the trust is responsible for paying the trustee's legal fees.

The fact that a trust instrument allows a trustee to hire lawyers does not give the trustee a blank check. The legal fees incurred will still need to be reasonable to accomplish the purpose of the trust and defend the trustee. And if the trustee loses in litigation, particularly if the claim was for a breach of fiduciary duty, a beneficiary may surcharge the trustee to try to recover the decreased value of the trust resulting from the breach, which may include a reimbursement of the trustee's legal fees. In some instances, a beneficiary may even seek a court order prohibiting a trustee from defending itself using trust funds. Those requests, which are similar to seeking a preliminary injunction, are difficult to win and should be reserved for rare circumstances involving significant evidence of intentionally wrongful conduct, not as leverage in run-of-the-mill disputes between a beneficiary and a trustee.

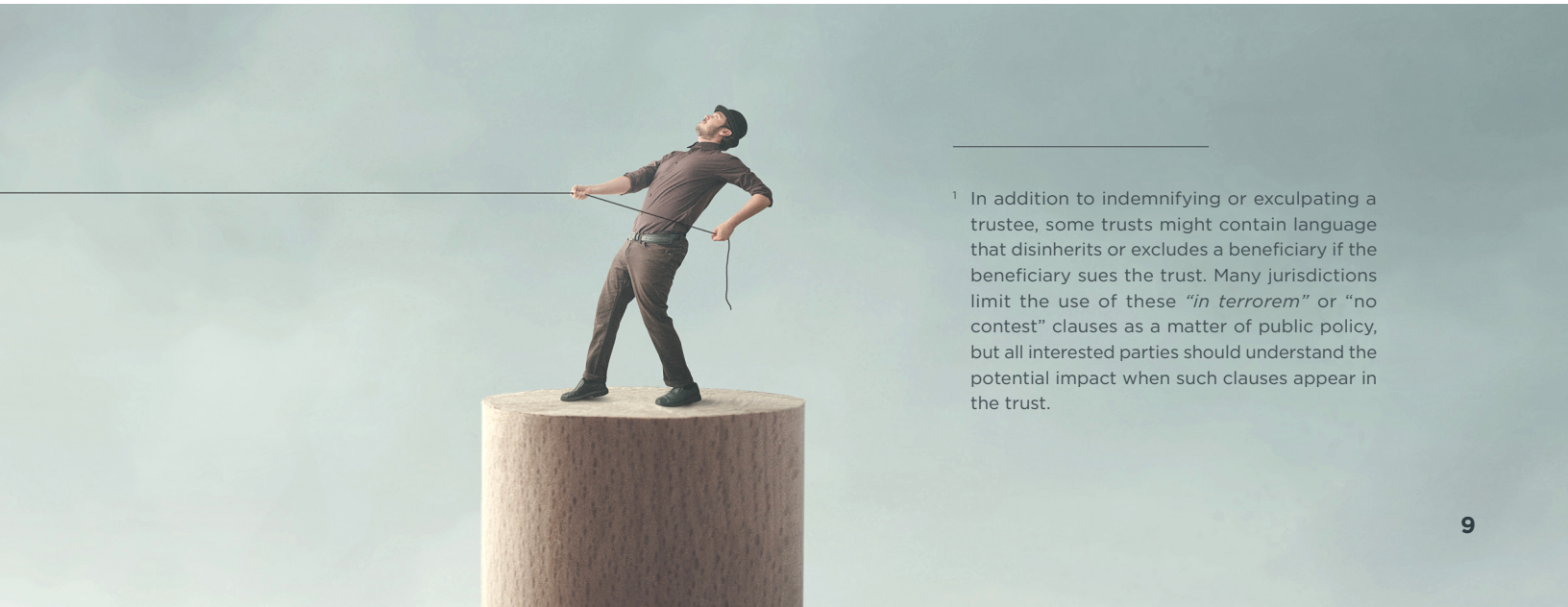
Beneficiaries or others involved in trust litigation can sometimes recover their legal fees from the trust as well. To do so, the party asking for reimbursement generally must show that the litigation was of significant benefit to the trust—whether by recouping money lost, removing a fiduciary who is a bad actor, or otherwise preserving the assets of the trust. The standard for recovery will vary based on the trust instrument and on the law of the jurisdiction in question and is often discretionary and fact-dependent. That is why a beneficiary should not assume the trust will foot the bill for legal fees.

Beneficiaries—even beneficiaries with a significant net worth—may also lack direct access to assets to pay legal fees. And even if a beneficiary can pay lawyers, those expenses might take up resources that would be used to pay other expenses. Beneficiaries may end up making additional requests for distributions from the trust—whether explicitly for legal fees, or to make up other shortfalls resulting from legal bills. While a trustee might be tempted to cut off all distributions to a beneficiary when the beneficiary is suing the trust, it is often better to consider such distribution requests in the ordinary course of business independent of the litigation. Ultimately, an exercise of discretion that is not tied to litigation positions is more likely to be upheld.

A final backstop is the equitable power of a supervising court. In instances where a trust instrument is vague or where circumstances are particularly compelling, a court can determine whether the trust should pay (or not pay) legal bills as a matter of equity. Like with other discretionary requests, no trustee or beneficiary should assume that a court will invoke its equitable authority to order payment of legal bills.

Some trusts have so much money that legal bills do not put a dent in them. But for most trusts, legal fees from a protracted fight can significantly reduce the assets available for supporting beneficiaries. All sides should be aware of how legal fees might be paid in a dispute and should continue to evaluate the payment of fees as the dispute evolves. And if you have questions or concerns about payment of legal fees or a trust dispute, please do not hesitate to contact one of our Wealth Planning and Fiduciary Disputes attorneys.

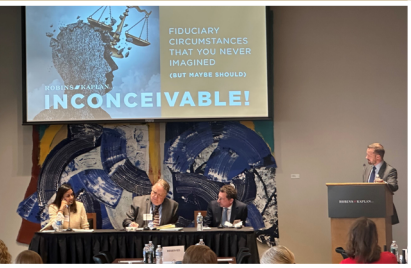
TIM BILLION represents clients in a wide variety of cases, including trust and fiduciary litigation, contract and fraud claims, and earn-out disputes.

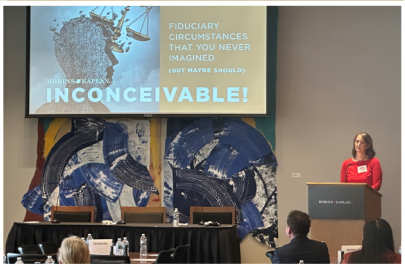


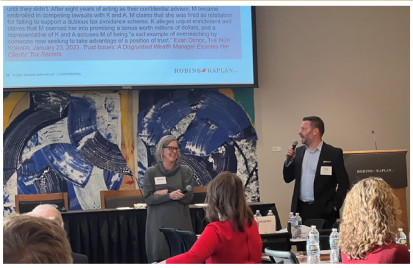
[1] In addition to indemnifying or exculpating a trustee, some trusts might contain language that disinherits or excludes a beneficiary if the beneficiary sues the trust. Many jurisdictions limit the use of these *"in terrorem"* or "no contest" clauses as a matter of public policy, but all interested parties should understand the potential impact when such clauses appear in the trust.

INCONCEIVABLE!

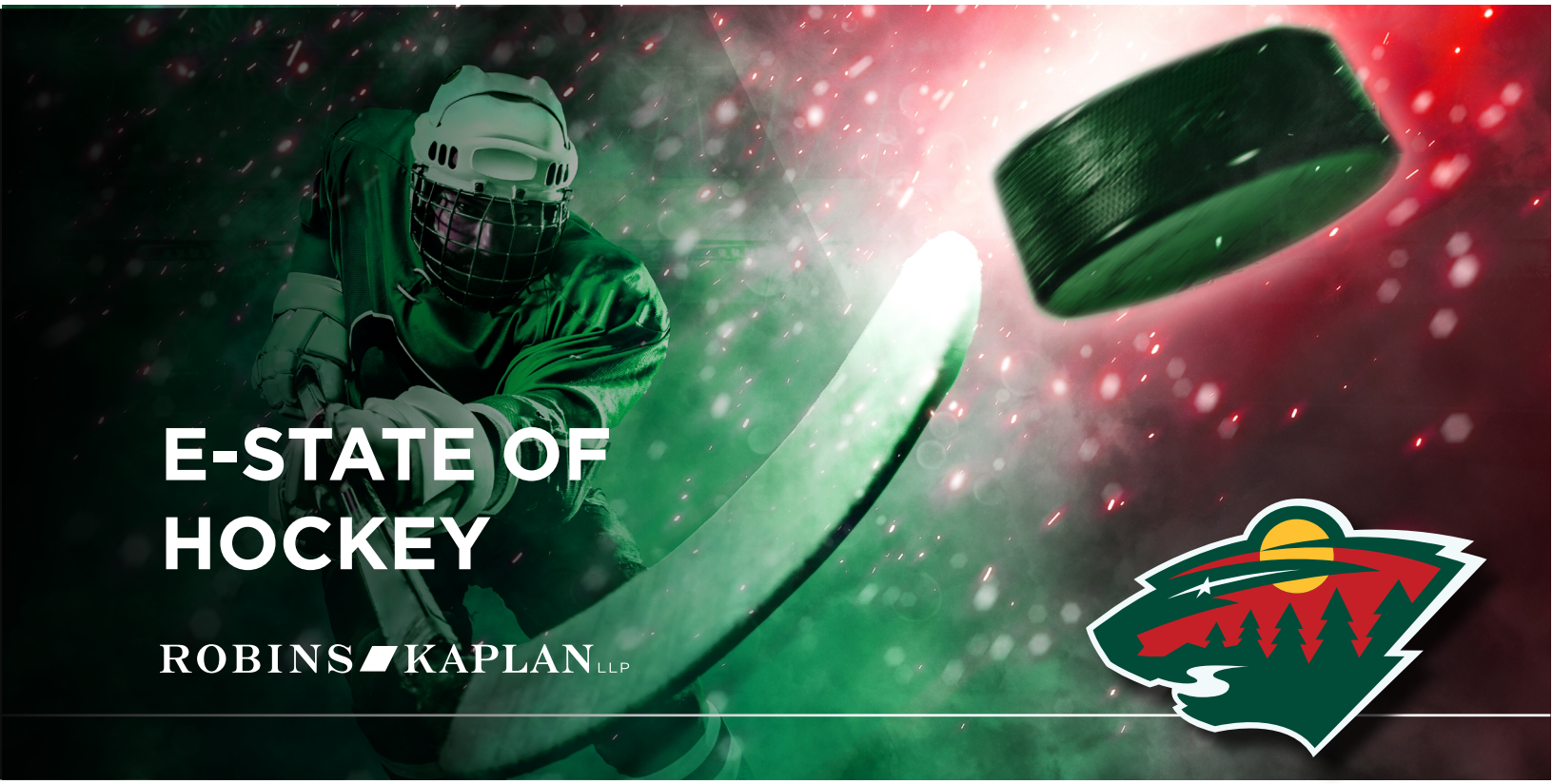
FIDUCIARY CIRCUMSTANCES THAT YOU NEVER IMAGINED **(BUT MAYBE SHOULD)**







Thank you to everyone who joined us for an afternoon of reflections, discussions, and lessons learned at our 2023 Wealth Disputes Seminar titled, "Inconceivable! Fiduciary Circumstances That You Never Imagined (But Maybe Should)." We hope you found the programming helpful and engaging. A special thanks to our esteemed speakers, Thomas Simmons, Suma Nair, Judge Edward Wahl, and Katie Engelhart, for taking the time to share valuable insights with our attendees.



The Robins Kaplan Wealth Planning, Administration, and Fiduciary Disputes Group is going to watch the Minnesota Wild play the Pittsburgh Penguins in St. Paul on February 9, 2024. Call Anne Lockner at 612-349-8470 if you are interested in joining us.

MEET OUR ISSUE EDITOR:

DANIEL ALLENDER

DANIEL ALLENDER is a trial attorney who navigates high-stakes disputes across industries, with an emphasis on retail, real estate, and technology companies. Daniel regularly represents both plaintiffs and defendants in commercial and intellectual property matters and complex matters involving property insurance litigation and insurance coverage.

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ANNE M. LOCKNER

ANNE LOCKNER is a seasoned partner in the firm's National Business Litigation Group and a member of the Executive Board. Experienced in a variety of areas including breaches of fiduciary duties among shareholders, breaches of contract, fraud, trade secret misappropriation, and non-compete cases, Anne is known for her strategic guidance to business leaders facing complex disputes. With extensive trial experience and a focus on early resolutions, she brings a pragmatic approach to litigation.

Recognized widely for her professional accomplishments, Anne has been named a "Litigation Star" by Benchmark Litigation, a "Minnesota Super Lawyer" by Super Lawyers, and listed in The Best Lawyers in America for over a decade. Additionally, she was recently named to Lawdragon's "500 Leading Litigators in America" guide, honoring attorneys whose "sustained excellence in trials is nothing short of remarkable."

Anne's commitment to justice is evident in her five-year leadership of the firm's pro bono program and her representation of asylum seekers, foster children, domestic abuse survivors, and veterans. Beyond her legal work, Anne is actively involved in community service, serving on boards including The Children's Theater Company and The Advocates for Human Rights. She currently serves as Chair of The Fund for Legal Aid, the fundraising arm of Mid-Minnesota Legal Aid.

In her free time, Anne enjoys watching her twin daughters (learn to) play volleyball, listening to them (learn to) play clarinet and flute, watching baking shows with her husband and daughters, and reading a variety of books—both fiction and non-fiction.

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