SUPREME COURT OF THE STATE OF NEW YORK, APPELLATE DIVISION, SECOND DEPARTMENT

Bauer v. Bauernschmidt

187 A.D.2d 477 (2d Dep't 1992) · Decided November 9, 1992

SUMMARY

The court reviewed surcharges imposed against a trustee for alleged mismanagement of two inter vivos trusts. It held that the trustee generally acted in good faith and with adequate prudence, but affirmed a reduced surcharge of $2,500 for each trust based on improper capital expenditures from trust funds that the trustee personally enjoyed.

CASE DETAILS

COURT	Supreme Court of the State of New York, Appellate Division, Second Department
WRITING FOR THE COURT	Bracken, J.P.; Harwood, J.; Balletta, J.; Fiber, J.
JURISDICTION	New York
DECIDED	November 9, 1992
DISPOSITION	remanded
PROCEDURAL POSTURE	The trustee appealed from a judgment entered after a nonjury trial in an action to compel an accounting and impose surcharges for alleged trust mismanagement.
STANDARD OF REVIEW	The court reviewed the trustee's surcharge liability and exercised its discretion to modify the amount of the award based on the record, the trust instrument, the settlor's intent, and the circumstances surrounding the expenditures.
PRECEDENTIAL VALUE	Published New York Appellate Division decision
PARTIES	Bauernschmidt v. Bauer

TOPICS

trust administration · trustee duties · breach of trust · damages · appellate procedure

PRACTICE AREAS

trusts and estates · fiduciary litigation · appellate procedure

QUESTIONS PRESENTED

1. Whether the trustee's inability to provide a satisfactory accounting established negligence or a failure to exercise the degree of care required to support a surcharge.
2. Whether the trust's exculpatory provision and informal-accounting provision were valid and limited the trustee's liability.
3. Whether the trial court's $21,985 surcharge for each trust was warranted under the circumstances.
4. Whether the trustee's $2,500 capital expenditures from each trust constituted an improper appropriation of trust property.

HOLDINGS

1. A surcharge requires proof that a financial loss resulted from the trustee's negligence or failure to exercise the degree of care employed by prudent persons of discretion and intelligence in similar affairs.
2. An exculpatory provision in an inter vivos trust relieving a trustee from liability for good-faith conduct is valid so long as there is some accountability, at least to the settlor.
3. Whether a surcharge should be imposed for a particular investment or expenditure depends on the circumstances of the individual case, including the settlor's intent, the parties' relationship, and the history of the investment viewed when the challenged act or omission occurred.
4. The trustee was properly surcharged $2,500 from each trust because those capital expenditures constituted an improper personal appropriation of trust property.

KEY QUOTATIONS

> *“To warrant a surcharge, the plaintiffs must show that a financial loss resulted from the defendant’s negligence or failure to exercise that degree of care which " 'prudent [people] of discretion and intelligence in such matters, employ in their own like affairs’ ””* (478)

> *“Furthermore, whether a surcharge is to be imposed for a particular investment decision must necessarily depend on the circumstances of each case, including the settlor’s intent, the relationship of the parties, and the history of the particular investment viewed at the time of the act or failure to act for which the surcharge is imposed”* (479)

FACTUAL BACKGROUND

The defendant served as trustee of two inter vivos trusts established for his daughters, each funded with approximately $18,000. The trust instrument gave him broad investment discretion and relieved him of liability for acts or omissions undertaken in good faith, while permitting informal accountings to the settlor. The settlor knew of and tacitly approved expenditures for horses used by the beneficiaries, but the trustee also made $2,500 in capital expenditures from each trust whose benefits he personally continued to enjoy after the trusts ended.

PROCEDURAL HISTORY

The Supreme Court, Suffolk County, directed the trustee to pay a $21,985 surcharge for each of two trusts. The Appellate Division modified the judgment by reducing the surcharge for each trust to $2,500 with interest from

January 1, 1976, affirmed as modified, and remitted the matter for entry of an amended judgment.

DISPOSITION

remanded

REMAND INSTRUCTIONS

The matter was remitted to the Supreme Court, Suffolk County, for entry of an appropriate amended judgment reflecting a $2,500 surcharge for each trust, with interest from January 1, 1976.

CASES CITED

- Matter of Hahn, 93 A.D.2d 583, 586, aff'd, 62 N.Y.2d 821
- King v. Talbot, 40 N.Y. 76, 86
- Matter of Bank of N.Y., 35 N.Y.2d 512, 518-519
- Matter of Clark, 257 N.Y. 132, 136
- Matter of Kassover, 124 Misc. 2d 630
- Matter of Cowles, 22 A.D.2d 365, aff'd, 17 N.Y.2d 567
- Kolentus v. Avco Corp., 798 F.2d 949, 966, cert. denied, 479 U.S. 1032
- Matter of Levy, 97 Misc. 2d 582, 591

OPINION

PER CURIAM.

In an action to compel an accounting by the defendant as trustee of the Valerie *478Bauernschmidt Trust and the Claudia Bauernschmidt Trust, the defendant appeals from a judgment of the Supreme Court, Suffolk County (D’Amaro, J.H.O.), dated July 13, 1990, which, after a nonjury trial, directed him to pay, as a surcharge for the mismanagement of the trusts, the sum of $21,985 for each trust.

Ordered that the judgment is modified, as a matter of discretion, by reducing the amount awarded to each plaintiff from the principal sum of $21,985, to the principal sum of $2,500, with interest from January 1, 1976; as so modified, the judgment is affirmed, without costs or disbursements, and the matter is remitted to the Supreme Court, Suffolk County, for entry of an appropriate amended judgment.

The trust instrument pursuant to which the defendant acted granted him the power to invest and reinvest trust funds of approximately $18,000 on behalf of each of the plaintiffs, his daughters, as he in his absolute judgment and discretion deemed in their best interests.

Moreover, the trust instrument provided that he was not to be held liable for any act or failure to act where he acted in good faith. The trust instrument authorized him to render informal accountings to the trusts’ settlor (his mother and the plaintiffs’ grandmother), in lieu of any formal accounting.

The settlor confirmed through her trial testimony that the defendant was to have absolute discretion over the use of the trust funds and she acknowledged that the expenditure of trust funds for the purchase and maintenance of horses for her granddaughters’ enjoyment and recreation was with her knowledge and tacit approval.

The trial court determined, however, that the defendant’s inability to satisfactorily account for his expenditures on behalf of the plaintiffs constituted evidence that he mismanaged the funds entrusted to him and it imposed a surcharge payable to each plaintiff exceeding the original value of each trust.

To warrant a surcharge, the plaintiffs must show that a financial loss resulted from the defendant’s negligence or failure to exercise that degree of care which " 'prudent [people] of discretion and intelligence in such matters, employ in their own like affairs’ ” (Matter of Hahn, 93 AD2d 583, 586, affd 62 NY2d 821, quoting from King v Talbot, 40 NY 76, 86; Matter of Bank of N. Y., 35 NY2d 512, 518-519; Matter of Clark, 257 NY 132, 136).

While the essential ingredient of a trust is the accountability of the trustee (see, Matter of Kassover, 124 Misc 2d 630), exculpatory provisions like those in the present case are valid in inter vivos trusts so long as there is *479some accountability, at least to the settlor (cf., Matter of Kassover, supra; see also, Matter of Cowles, 22 AD2d 365, affd 17 NY2d 567; see also, Kolentus v Avco Corp., 798 F2d 949, 966, cert denied 479 US 1032).

Furthermore, whether a surcharge is to be imposed for a particular investment decision must necessarily depend on the circumstances of each case, including the settlor’s intent, the relationship of the parties, and the history of the particular investment viewed at the time of the act or failure to act for which the surcharge is imposed (see, Matter of Bank of N. Y., supra; cf., Matter of Levy, 97 Misc 2d 582, 591).

Against the backdrop of the settlor’s intent and the nature of the relationship of all the parties during the life of the trust, the record establishes that the defendant generally acted in good faith and with the requisite degree of diligence and prudence (see, e.g., Matter of Bank of N. Y., supra, at 519).

We thus regard the surcharges imposed by the Supreme Court as unwarranted. However, the defendant made capital expenditures of $2,500 from each trust, the fruits of which he now personally enjoys even though the trusts have not existed since 1976. Those expenditures constituted an improper appropriation of trust property.

Thus, we modify the surcharges as indicated. We have considered the defendant's remaining contentions and find them either to be unpreserved for appellate review (see, CPLR 5501 [a] [3]), or without merit. Bracken, J. P., Harwood, Balletta and Fiber, JJ., concur.