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## A Judicial and Economic Analysis of Attorney's Fees in Trust Litigation and the Resulting Inequitable Treatment of Trust Beneficiaries.

Charles Epps Ipock

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## COMMENT

### A JUDICIAL AND ECONOMIC ANALYSIS OF ATTORNEY'S FEES IN TRUST LITIGATION AND THE RESULTING INEQUITABLE TREATMENT OF TRUST BENEFICIARIES

CHARLES EPPS IPOCK

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## I. INTRODUCTION

In traditional American civil litigation, two parties fight—the plaintiff and the defendant. The plaintiff sues the defendant for damages caused to the plaintiff.<sup>1</sup> However, an additional consideration is often at play—which party, if any, must pay attorney's fees.<sup>2</sup> Litigation involving attorney's fees is contentious at best, and often is as complex as the underlying matter.<sup>3</sup> However, wouldn't it be nice if there was a third-party entity, often valued at extremely high monetary figures, accessible to pay attorney's fees?<sup>4</sup> Texas courts have answered this question with an unequivocal yes.<sup>5</sup>

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1. See *Martin v. Trevino*, 578 S.W.2d 763, 772 (Tex. Civ. App.—Corpus Christi 1978, writ ref'd n.r.e.) (establishing that damages are a necessary element in a tort claim).

2. See *Smith v. Hennington*, 249 S.W.3d 600, 606 (Tex. App.—Eastland 2008, pet. denied) (considering the additional element of attorney's fees, which are often debated in matters extending far beyond trust litigation).

3. See *Donahue v. Donahue*, 105 Cal. Rptr. 3d 723, 726 (Ct. App. 2010) (portraying how contentious the award of attorney's fees can become when attorneys charge nearly \$700 an hour and accumulate fees close to \$5 million).

4. See *Ginther v. Bank of Am., N.A.*, No. 01-08-00430-CV, 2010 WL 2244098, at \*7

Trust litigation generally involves a trust beneficiary suing a trustee, and creates a relationship where a third-party entity, the trust, is present. At times, Texas courts will delve into this third-party entity to pay a negligent trustee's attorney's fees, even after a jury determines that the trustee has breached its duty of trust or fiduciary duty.<sup>6</sup> The invasion of trust funds to pay attorney's fees stems from sections 114.063 and 114.064 of the Texas Trust Code,<sup>7</sup> and case law prior to and after their codification. This Comment refers to this case law and statutory compilation as the "interplay." The net result of the interplay is the use of varying and vague judicial tests that often result in inequitable treatment of trust beneficiaries.

Imagine death strikes a teenager's family. Even though the teenager's parents were lost tragically, they previously established a trust to assist in the payment of college tuition and living expenses for their child. Just before college begins, the teenager receives word that his trust's value has surreptitiously dropped. The trustee's investment decisions have taken the trust, originally valued at \$50,000, to a mere \$10,000. The trustee's investments in the banking and car industries, which some believed would quickly rebound after the federal governmental bailouts, fail to produce a return. As a result, the teenager initiates a lawsuit against the trustee alleging breach of fiduciary duty.<sup>8</sup>

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(Tex. App.—Houston [1st Dist.] May 28, 2010, pet. denied) (mem. op.) (illustrating how valuable some trusts may be, and that the trust in question was valued at \$16 million).

5. Compare *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 220 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (holding that although the trustees acted improperly in administering the trust, their actions were "reasonable" and their attorney's fees should be paid from trust funds), with Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (summarizing the Texas case, *Hachar v. Hachar*, 153 S.W.3d 138 (Tex. App.—San Antonio 2004, no pet.), as a matter that "reminds litigants that any party involved in trust litigation should seek an award of attorney's fees under [Texas] Trust Code [s]ection 114.064 because the court has the authority to award fees even in favor of the losing party if the court believes that it is equitable and just" for such an award).

6. See *Grey v. First Nat'l Bank*, 393 F.2d 371, 387 (5th Cir. 1968) ("[A] trustee may charge his trust for attorney's fees which the trustee, acting reasonably and in good faith, incurs in defense of litigation charging him with a breach of trust."). Therefore, trust funds can be used to pay a negligent trustee's attorney's fees if the trustee acts reasonably in its defense. *Id.*

7. The Texas Trust Code is codified within Title 9, subtitle B of the Texas Property Code. TEX. PROP. CODE §§ 111.001–.206 (West 2007 & Supp. 2011). This Comment will use the term "Texas Trust Code" to refer to Title 9, subtitle B. *Id.* § 111.001.

8. See generally *id.* § 113.006 (applying the Uniform Prudent Investors Act, which provides the applicable fiduciary standards for trustee investment decisions).

The teenager establishes his claim and the trial is successful. Fortunately, the jury determines the applicable damages are \$40,000, which the trustee replenishes to the trust.<sup>9</sup> However, the trustee's defense against the suit proves expensive, and the trustee's attorney's fees reach \$20,000. A hearing is held to determine whether granting attorney's fees to the trustee from trust funds is appropriate. The court utilizes the current statutory provision applicable to attorney's fees in trust litigation—Trust Code section 114.064 and relevant case law.<sup>10</sup> The court determines that the trustee acted “reasonably and in good faith” in defending the suit, satisfying the common law test, and based on this determination, the court decides that it is equitable and just to award attorney's fees through the application of section 114.064.<sup>11</sup> Unfortunately for the teenager, the economic picture after winning his suit is grim. The trust started at \$50,000, but through the trustee's negligence, the trust dissipated to \$10,000. The trustee repaid the lost \$40,000 to the trust; however, due to the litigation, the court delved into trust funds and awarded \$20,000 in attorney's fees to the trustee, resulting in a final trust value of \$30,000. The net result after *winning* his suit is a loss of \$20,000 from the original trust value, 40% of the trust.

This Comment addresses the interplay of current trust law and asks how the law can be changed to remedy the inequities that trust beneficiaries may face in trust litigation. Part II details the concepts and principles of trusts that lay the foundation for understanding the structure, parties, and duties owed in a trust. Part III provides an in-depth judicial and economic analysis of case law and statutory provisions that describe the interplay's

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9. See generally *id.* § 114.001(c) (“A trustee who commits a breach of trust is chargeable with any damages resulting from such breach of trust . . .”).

10. See *id.* § 114.064 (“In any proceeding under this code the court may make such award of costs and reasonable and necessary attorney's fees as may seem equitable and just.”); see also *Grey*, 393 F.2d at 387 (reiterating the general principle established by case law, stating “a trustee may charge his trust for attorney's fees which the trustee, acting reasonably and in good faith, incurs in defense of litigation charging him with a breach of trust”).

11. *Grey*, 393 F.2d at 387. Compare PROP. § 114.064 (utilizing an “equitable and just” test in determining whether to grant attorney's fees), with *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 220 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (establishing the common law test for awarding attorney's fees to trustees in actions alleging trustee misconduct by looking at the reasonableness of the trustee's actions and whether the trustee acted in good faith).

inequities. Part IV addresses the multitude of reasons why the interplay matters and why it must be changed. Finally, Part V promulgates a remedy that alleviates the discriminatory results of the interplay.

## II. THE CONCEPTS AND PRINCIPLES OF TRUSTS

### A. *Development of Trust Principles*

The “ancestor of the modern[-]day trust,” referred to as the *use*, originated in England during the Middle Ages.<sup>12</sup> The *use* was instituted by King Henry V and modeled after the Roman devise called the *fideicommissum*.<sup>13</sup> “The *fideicommissum* was created . . . to circumvent the narrowness and rigidity of the *ius civile*,” which “prohibited [certain persons] from becoming beneficiaries of a legal testament.”<sup>14</sup> The *fideicommissum* allowed the testator to devise property to a person who could be an heir, while requesting the property be transferred to a person who was “legally incapable of being a direct beneficiary.”<sup>15</sup> “The Roman theory ranks as the earliest exposition of the origin of the trust and maintains that the *fideicommissum* was the direct ancestor of the English *use*.”<sup>16</sup> Importantly, both the *use* and the *fideicommissum* utilized the same legal design of transferring property through an intermediary to a third-party beneficiary.<sup>17</sup>

The modern-day trust also takes inspiration from cultures outside of Rome and England.<sup>18</sup> The fifth-century German tribe known as the Salian Franks provided inspiration by utilizing a system known as the *salmannus* in their judicial code, the *Lex Salica*, “which recognized a third party, the *salmannus*, to aid in

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12. AMY MORRIS HESS ET AL., *THE LAW OF TRUSTS AND TRUSTEES* § 2 (3d. ed. 2007).

13. See Avisheh Avini, Comment, *The Origins of the Modern English Trust Revisited*, 70 TUL. L. REV. 1139, 1148 (1996) (acknowledging that “the *fideicommissum* was the direct ancestor of the English *use*” (citing 2 WILLIAM BLACKSTONE, *COMMENTARIES* \*328)).

14. *Id.* at 1147.

15. *Id.*

16. *Id.* at 1148.

17. See *id.* (“Both institutions were designed to transfer property in the future through a third-party intermediary.”).

18. See *id.* at 1149–62 (comparing the structure and origin of the modern-day trust to the Salic Salmannus, the Romano–Germanic theory, and the Islamic Waqf).

the transfer of property.”<sup>19</sup> The custom “involved the *inter vivos* transfer of property to a *salmannus*, a person trusted to transfer the property to a designated beneficiary upon the death of the original transferor.”<sup>20</sup> Lastly, the Romano–Germanic theory hypothesizes inspiration for the modern-day trust was from a combination of German and Roman elements that contributed to the *use* and the subsequent development of the modern-day trust.<sup>21</sup>

### B. *Purposes of Trusts*

The Uniform Trust Code points out that the most important purpose of a trust is simple—“[a] trust and its terms must be for the benefit of its beneficiaries.”<sup>22</sup> The Texas Trust Code echoes this fundamental yet vital sentiment by stating that “[b]eneficiary” means a person for whose benefit property is held in trust, regardless of the nature of the interest.”<sup>23</sup> The most straightforward and essential consideration is that the purpose of a trust is to benefit its beneficiary.<sup>24</sup>

19. *Id.* at 1149.

20. *Id.*

21. *See id.* at 1151 (discussing elements of the modern-day trust that evolved as a collaboration between differing cultures).

22. UNIF. TRUST CODE § 404 (amended 2005), 7C U.L.A. 484 (2006); accord John H. Langbein, *Mandatory Rules in the Law of Trusts*, 98 NW. U. L. REV. 1105, 1119 (2004) (reiterating the Uniform Trust Code rules by stating that a trust and its terms are required to “be for the benefit of its beneficiaries” (citing UNIF. TRUST CODE § 412 cmt. (amended 2005), 7C U.L.A. 507–08 (2006) (internal quotation marks omitted)).

23. TEX. PROP. CODE ANN. § 111.004 (West Supp. 2011).

24. *See id.* (portraying that the purpose of a trust is to benefit the beneficiary). The Texas Trust Code’s use of the word “benefit” evidences a much larger purpose of trusts than solely a monetary benefit. *Id.* Undoubtedly, many trusts are solely for financial benefit, yet equally as many are not. Substantial numbers of testamentary trusts are created to provide for minor descendants who lack the legal capability or legal authority to manage property; thus, the trust is established to benefit the minor in the management of property. *See Thatcher v. Conway*, 296 S.W.2d 790, 795 (Tex. Civ. App.—Beaumont 1956, no writ) (providing that the will of the decedent “created a trust for the benefit of his minor son as sole beneficiary and appointed the appellees as trustees to carry out [decedent’s] wishes as expressed in the instrument”). Similarly, special-needs trusts are designed to provide for the “beneficiary’s ‘special,’ or ‘supplemental,’ needs.” Jennifer Field, Comment, *Special Needs Trusts: Providing for Disabled Children Without Sacrificing Public Benefits*, 24 J. JUV. L. 79, 81 (2004). The funds in a special-needs trust go “above and beyond” government benefits such as Supplemental Security Income (SSI) benefits, “which can greatly enhance a disabled child’s life.” *Id.* The special-needs trust again illustrates the concept that a trust is not merely a tool to provide monetary benefits, but a tool that provides benefits far exceeding that of money.

The Trust Code also adopts the rule that “[a] trust may be created for any purpose that is not illegal. The terms of the trust may not require the trustee to commit a criminal or tortious act or an act that is contrary to public policy.”<sup>25</sup> More specifically, the Internal Revenue Code provides that one purpose of trusts is to legally avoid taxes.<sup>26</sup> Some trusts function as “methods that can provide for the investment and management of the client’s assets during his lifetime or for their disposition upon the client’s death, or that accomplish both objectives.”<sup>27</sup> Trusts also function to avoid the burdens of asset management, avoid probate, and “protect . . . against unforeseen contingencies such as incompetency, incapacity, physical disability[,] or similar misfortune.”<sup>28</sup>

### C. *Revocable and Irrevocable Trusts and the Involved Parties*

Trusts are often categorized as revocable or irrevocable.<sup>29</sup> A revocable trust allows the settlor to “revoke the trust unless it is irrevocable by the express terms of the instrument creating it or of an instrument modifying it.”<sup>30</sup> The trustee of a revocable trust must comply with the direction of the settlor even though the direction is contrary to the terms of the trust or the trustee’s normal fiduciary duties “if the direction is communicated to the trustee in writing in a manner by which the settlor could properly

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25. PROP. § 112.031 (West 2007).

26. *See* I.R.C. § 643(f)(2) (2006) (acknowledging that the “principal purpose of such trusts is the avoidance of the tax imposed”). The Internal Revenue Code provides a multitude of avenues to create trusts to “decreas[e] the amount of federal estate taxes that may be incurred by a family.” 1 GEORGE M. TURNER, IRREVOCABLE TRUSTS § 2:22 (3d ed., 2007). One example is the generation-skipping trust, which “seems, on the surface, to be a very simple transfer tax that is imposed in situations where a gift is made—either during life time or upon the death of an individual—to someone two generations below the transferor.” *Id.* § 21:2. *See generally* I.R.C. § 2621(a) (2006) (“[T]he taxable amount in the case of any taxable distribution shall be . . . the value of the property received by the transferee, reduced by . . . any expense incurred by the transferee in connection with the determination, collection, or refund of the tax imposed by this chapter with respect to such distribution.”).

27. AMY MORRIS HESS ET AL., THE LAW OF TRUSTS AND TRUSTEES § 231 (3d ed. 2007).

28. *Id.*

29. *Cf., e.g.*, PROP. § 112.051(a) (West 2007) (describing irrevocable trusts).

30. *Id.* *See generally* RESTATEMENT (SECOND) OF TRUSTS § 3(1) (1959) (defining the settlor as the person who creates the trust).



amend or revoke the trust.”<sup>31</sup> As a result, the rights of a beneficiary “are exercisable by and subject to the control of the settlor.”<sup>32</sup> Thus, the Restatement (Third) of Trusts considers that, while the trust is revocable, “the settlor may enforce the trust on behalf of all beneficiaries, and the trustee’s duties are owed primarily to the settlor, or solely to the settlor insofar as the rights of other beneficiaries are preempted by conduct of the settlor.”<sup>33</sup> The Uniform Trust Code also states clearly that “[w]hile a trust is revocable . . . duties of the trustee are owed exclusively to[] the settlor.”<sup>34</sup>

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31. RESTATEMENT (THIRD) OF TRUSTS § 74(1)(a)(i) (2007); *accord* RESTATEMENT (SECOND) OF TRUSTS § 3(3) (1959) (defining the trustee as the party holding the property in trust).

32. RESTATEMENT (THIRD) OF TRUSTS § 74(1)(b) (2007); *accord* RESTATEMENT (SECOND) OF TRUSTS § 3(4) (1959) (defining the beneficiary as the party who the trust is benefiting).

33. RESTATEMENT (THIRD) OF TRUSTS § 74 cmt. e (2007).

34. UNIF. TRUST CODE § 603(a) (amended 2005), 7C U.L.A. 553 (2006); *see* Jeramie Fortenberry, *Trustee's Duty to Beneficiaries of Revocable Trust*, FORTENBERRY LEGAL (July 27, 2010), <http://www.fortenberrylaw.com/blog/raines-synovus/> (asking the question of whether a trustee owes fiduciary duties to beneficiaries of revocable trusts). In *Ex parte Synovus Trust Co.*, the Alabama Supreme Court construed a state statute commenting “[w]hile a trust is revocable, rights of the beneficiaries are subject to the control of, and the duties of the trustee are owed exclusively to, the settlor.” 41 So. 3d 70, 74 (Ala. 2009) (quoting ALA. CODE § 19-3B-603 (2007)) (internal quotation marks omitted); *accord* Jeramie Fortenberry, *Trustee's Duty to Beneficiaries of Revocable Trust*, FORTENBERRY LEGAL (July 27, 2010), <http://www.fortenberrylaw.com/blog/raines-synovus/> (discussing the Alabama Supreme Court’s ruling in *Synovus Trust*). According to one commentator, the statute’s clear language led the Alabama Supreme Court to have little trouble in establishing the plain meaning of the rule. Jeramie Fortenberry, *Trustee's Duty to Beneficiaries of Revocable Trust*, FORTENBERRY LEGAL (July 27, 2010), <http://www.fortenberrylaw.com/blog/raines-synovus/>. Conceptually, many laypersons and attorneys assume the duties of trustees run to the trust beneficiaries; however, “[j]ust as a person can freely amend his or her will without liability to the named beneficiaries, the settlor/trustee of a revocable trust should be able to manage and change his or her trust without liability to the beneficiaries.” *Id.* Put another way, “both wills and revocable trusts are ambulatory instruments, meaning that they can be freely amended without liability to anyone while the person who established them is alive. The Alabama statute is a legislative recognition of this general principle.” *Id.* Grasping the concept of what parties are owed which duties assists in understanding *Moon v. Lesikar*, decided by the Texas Fourteenth Court of Appeals in 2007. 230 S.W.3d 800 (Tex. App.—Houston [14th Dist.] 2007, pet. denied). A beneficiary of a revocable trust brought suit alleging numerous causes of action, one of which was breach of fiduciary duty against the trustee. *Id.* at 802. The court provided that the contingent beneficiary “would appear to meet the definition of an interested person with standing to bring suit against a trustee for breach of fiduciary duty. However, Mr. Lesikar, as settlor, was empowered to revoke or amend the . . . [t]rust.” *Id.* at 803. The court opined that the question on point was “whether a

However, irrevocable trusts feature different treatment. When a settlor creates a revocable trust during his or her lifetime, and does not revoke it prior to death, the trust becomes irrevocable.<sup>35</sup> Similarly, a testamentary trust created in a decedent's will is irrevocable because the decedent cannot revoke the trust after death.<sup>36</sup> An irrevocable trust also establishes a fiduciary relationship between the trustee and the beneficiary.<sup>37</sup> The scope of this Comment extends only to irrevocable trusts.

#### D. *The Interrelationship Between the Parties of a Trust*

A trust is best thought of as a three-tiered entity: at the top of the entity is the trustee, in the middle is the trust corpus or principal, and at the bottom are the trust beneficiaries.<sup>38</sup> The interrelationship between the parties creates a multitude of rules that are some of the most stringent in all of law.<sup>39</sup> The

contingent beneficiary can complain of a transaction by the settlor of a revocable trust, prior to the vesting of her interest upon the death of the settlor. By the cases the parties have cited and our own research, it does not appear that Texas has addressed this issue." *Id.* The court analyzed cases from New York, Florida, and Iowa, and came to the conclusion that because the beneficiary's interests were subject to the settlor's discretion before his death, the trustee's fiduciary duties did not run to the beneficiary. *Id.* at 804. The sentiment is echoed in *Probate & Property*, which summarizes the rule of revocable trusts contained in *Moor*: "A beneficiary has no standing to challenge the actions of a trustee while the settlor can revoke." Gerry W. Beyer, *Keeping Current—Probate, PROB. & PROP.*, Mar./Apr. 2008, at 17–18.

35. See *Citizens Nat'l Bank of Breckenridge v. Allen*, 575 S.W.2d 654, 658 (Tex. Civ. App.—Eastland 1978, writ ref'd n.r.e.) ("[W]hen a valid inter vivos revocable trust is established and not revoked during the lifetime of the trustor, it becomes irrevocable upon his death . . .").

36. See TEX. PROP. CODE ANN. § 112.051(a) (West 2007) (stating "[a] settlor may revoke the trust," which implies that the settlor must be living to revoke a trust).

37. See *Huie v. DeShazo*, 922 S.W.2d 920, 921 (Tex. 1996) (acknowledging the fiduciary duties a trustee owes the beneficiary through an irrevocable trust); see also *Grey v. First Nat'l Bank*, 393 F.2d 371, 376 (5th Cir. 1968) (acknowledging the fiduciary obligation that existed between the trustee and beneficiary of an irrevocable trust).

38. See RESTATEMENT (SECOND) OF TRUSTS § 17(c) (1959) ("A trust may be created by . . . a transfer by will by the owner of property to another person as trustee for a third person . . ."). See generally *Westerfeld v. Huckaby*, 474 S.W.2d 189, 192 (Tex. 1971) (providing that the parties involved in the three-tiered entity can vary in that "[t]he trust act also permits the settlor to hold property as trustee for another, or for himself and another").

39. Detailing the obligations of trustees, Justice Cardozo stated that "[a] trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this[,] there has developed a tradition that is unbending and inveterate." *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928). Texas courts have reiterated Justice Cardozo's sentiment.

relationship between the beneficiary and the trustee is known as a fiduciary relationship.<sup>40</sup> Texas courts have long recognized a fiduciary relationship between the parties as a matter of law.<sup>41</sup> Accordingly, the fiduciary relationship requires the trustee to act with “an unwavering duty of good faith, fair dealing, loyalty[,] and fidelity over the affairs of the trust and its corpus.”<sup>42</sup> The trustee’s relationship with the “trust estate is personal and one of confidence. He handles another’s property. The law ought and does demand of him a strict accounting to the letter and spirit of his contract. It tolerates no deviation therefrom [that] amounts to a breach of his agreement.”<sup>43</sup> Furthermore, these standards place a burden upon the trustee that “[e]very violation by a trustee of a duty which equity lays on him, whether wilful or forgetful, is a breach of trust, for which he is liable.”<sup>44</sup>

The trustee, at a minimum, has fundamental duties that “include the use of the skill and prudence which an ordinary[,] capable[,] and careful person [would] use in the conduct of his own affairs, and loyalty to the beneficiaries of the trust.”<sup>45</sup> The trustee also must carry out the express terms of the trust; failure to do so constitutes a breach of trust.<sup>46</sup> Reiterating the high level of scrutiny placed on fiduciaries, “[a] trustee commits breach of trust not only where he violates a duty in bad faith, or intentionally although in good faith, or negligently[,] but also where he violates a duty because of a mistake.”<sup>47</sup>

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*See Lopez v. Munoz, Hockema & Reed, L.L.P.*, 22 S.W.3d 857, 866 (Tex. 2000) (echoing Justice Cardozo’s strong conviction for the obligations of fiduciaries).

40. *See Huie*, 922 S.W.2d at 921 (asserting that trustees owe fiduciary duties to trust beneficiaries).

41. *See Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 199 (Tex. 2002) (“Fiduciary duties are imposed by courts on some relationships because of their special nature. . . . Our courts have long recognized that certain fiduciary duties are owed by a trustee to a beneficiary of the trust . . . .” (citation omitted)).

42. *Ames v. Ames*, 757 S.W.2d 468, 476 (Tex. App.—Beaumont 1988, writ granted), *aff’d*, 776 S.W.2d 154 (Tex. 1989).

43. *Republic Nat’l Bank & Trust Co. v. Bruce*, 105 S.W.2d 882, 885 (Tex. 1937).

44. *Id.*

45. *InterFirst Bank Dall., N.A. v. Risser*, 739 S.W.2d 882, 888 (Tex. App.—Texarkana 1987, no writ) (citation omitted), *overruled on other grounds by Tex. Commerce Bank, N.A. v. Grizzle*, 96 S.W.3d 240 (Tex. 2002).

46. *See In re Watson*, 325 B.R. 380, 388 (Bankr. S.D. Tex. 2005) (“A trustee commits a breach of trust if he fails to carry out the express terms of a trust.” (citing *Griffin v. Hale*, 131 Tex. 152, 112 S.W.2d 1042, 1044 (1938))).

47. *Ertel v. O’Brien*, 852 S.W.2d 17, 21 (Tex. App.—Waco 1993, writ denied), *aff’d*

Additionally, trustees have a duty to disclose any material facts to the beneficiary, even if the relationship between the parties is strained.<sup>48</sup> The Trust Code and case law also indicate that a trustee must account to the beneficiary for each trust transaction.<sup>49</sup> Common law recognizes a “general prohibition against the fiduciary’s using the relationship to benefit his personal interest, except with the full knowledge and consent of the principal,” known as a prohibition against self-dealing.<sup>50</sup> A parallel prohibition is the commingling of funds. Courts articulate that “[a]ll transactions between the fiduciary and his principal are presumptively fraudulent and void, which is merely to say that the burden lies on the fiduciary to establish the validity of any particular transaction in which he is involved.”<sup>51</sup> While not an exhaustive list of the fiduciary duties owed by a trustee to a beneficiary, these duties illustrate a trustee’s burden and the opportunities for a trustee to breach the duties owed.

The distinction between equitable and legal title is also important.<sup>52</sup> It is undisputed in Texas that upon creation of a trust, “the beneficiaries become the owners of the equitable or

*sub nom.* Citizens Bank & Trust Co. of Baytown v. Ertel, No. 01-98-00548-CV, 2001 WL 26141 (Tex. App.—Houston [1st Dist.] Jan. 11, 2001, pet. denied) (not designated for publication).

48. See *Montgomery v. Kennedy*, 669 S.W.2d 309, 313 (Tex. 1984) (expressing that “[f]rom the earliest times, this court has written that, in the context of a fiduciary’s duty of full disclosure,” it extends even though there is an “existence of strained relations between the parties”).

49. See TEX. PROP. CODE ANN. § 113.151(a) (West 2007) (“[C]ourt[s] may require the trustee to deliver a written statement of account to all beneficiaries on finding that the nature of the beneficiary’s interest in the trust or the effect of the administration of the trust on the beneficiary’s interest is sufficient to require an accounting by the trustee.”); see also *Huie v. DeShazo*, 922 S.W.2d 920, 923 (Tex. 1996) (interpreting Trust Code section 113.151 as “requiring [the] trustee to account to beneficiaries for all trust transactions”).

50. *Chien v. Chen*, 759 S.W.2d 484, 495 (Tex. App.—Austin 1988, no writ). See generally *InterFirst*, 739 S.W.2d at 899 (“[S]elf-dealing is broader than the conduct prohibited by statute, as previously discussed, any conduct by the trustee which violates [a] fiduciary duty by taking advantage of the trustee’s position as trustee to benefit the trustee or some third person which the trustee desires to be benefited, can constitute self-dealing.”).

51. *Chien*, 759 S.W.2d at 495.

52. See *Faulkner v. Bost*, 137 S.W.3d 254, 258–59 (Tex. App.—Tyler 2004, no pet.) (distinguishing between the two titles by clarifying that legal title allows the trustee to hold the property “for the benefit of the beneficiaries” while equitable title allows one to actually benefit from the property).

beneficial title to the trust property and are considered the real owners.”<sup>53</sup> Put differently, the beneficiary “has true equitable title as against the trustee, who is a mere holder of the naked legal title at the convenience of the beneficiary.”<sup>54</sup> The net result of this distinction is that if trust assets are depleted, the beneficiary, as the equitable owner, not the trustee, as the legal holder, is the injured party.<sup>55</sup>

#### E. *The Remedies Available to a Beneficiary When a Trustee Breaches Fiduciary Duties*

The trustee’s broad prohibitions in the capacity as a fiduciary are equally matched by the broad areas of recourse that a beneficiary has in remedying the wrong. To prove that a fiduciary duty has been breached, the beneficiary must prove: “(1) a fiduciary relationship between the plaintiff and defendant, (2) a breach by the defendant of his fiduciary duty to the plaintiff, and (3) an injury to the plaintiff or benefit to the defendant as a result of the defendant’s breach.”<sup>56</sup>

When a breach of fiduciary duty occurs, potential remedies for a beneficiary include fee forfeiture,<sup>57</sup> rescission,<sup>58</sup> money damages with the possibility of exemplary damages,<sup>59</sup> imposition of a constructive trust,<sup>60</sup> and injunctive relief.<sup>61</sup> Also, a beneficiary can attempt to be made whole by recovering for any loss caused by a trustee’s breach of fiduciary duty.<sup>62</sup> Lastly, a beneficiary can file suit to remove the trustee.<sup>63</sup>

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53. *Id.* at 258 (quoting *City of Mesquite v. Malouf*, 553 S.W.2d 639, 644 (Tex. Civ. App.—Texarkana 1977, writ ref’d n.r.e.)) (internal quotation marks omitted).

54. *Hall v. Rawls*, 188 S.W.2d 807, 815 (Tex. Civ. App.—Beaumont 1945, writ ref’d w.o.m.).

55. *Cf. Shearrer v. Holley*, 952 S.W.2d 74, 78 (Tex. App.—San Antonio 1997, no writ) (stating that “[i]t is basic trust law” for legal and beneficial title to be separated).

56. *Lundy v. Masson*, 260 S.W.3d 482, 501 (Tex. App.—Houston [14th Dist.] 2008, pet. denied).

57. *Kinzbach Tool Co. v. Corbett–Wallace Corp.*, 138 Tex. 565, 160 S.W.2d 509, 514 (1942).

58. *Wils v. Robinson*, 934 S.W.2d 774, 782 (Tex. App.—Houston [14th Dist.] 1996), *vacated pursuant to settlement*, 938 S.W.2d 717 (Tex. 1997).

59. *Hawthorne v. Guenther*, 917 S.W.2d 924, 936 (Tex. App.—Beaumont 1996, writ denied).

60. *Thigpen v. Locke*, 363 S.W.2d 247, 252 (Tex. 1962).

61. *DSC Commc’ns Corp. v. Next Level Commc’ns*, 107 F.3d 322, 328 (5th Cir. 1997).

62. *See* TEX. PROP. CODE ANN. § 114.001(c) (West 2007) (“A trustee who commits breach of trust is chargeable with any damages resulting from such breach of trust . . .”);

### III. RECOVERY OF ATTORNEY'S FEES IN TRUST LITIGATION<sup>64</sup>

#### A. *Establishment of the Good Faith and Reasonableness Test and Its Inequity*

*Mitchell v. Mitchell*<sup>65</sup> and its ancillary proceeding, *American National Bank of Beaumont v. Biggs*,<sup>66</sup> illustrate how the acting

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see also RESTATEMENT (SECOND) OF TRUSTS § 205 (1959) (concurring that “if the trustee commits a breach of trust, he is chargeable with any loss . . . in value of the trust estate resulting from the breach of trust”).

63. See *Lee v. Lee*, 47 S.W.3d 767, 790 (Tex. App.—Houston [14th Dist.] 2001, pet. denied) (warning that an award of damages from the jury for a finding of a breach of fiduciary duty by a trustee constitutes grounds for a beneficiary to remove the trustee).

64. A vital distinction between whether to allow attorney's fees and the amount of attorney's fees to award is in order. Regarding attorney's fees, “the reasonable and necessary requirements [of the amount to award] are questions of fact to be determined by the fact finder, but the equitable and just requirements [of whether to grant attorney's fees] are questions of law for the trial court to decide.” *Hachar v. Hachar*, 153 S.W.3d 138, 142 (Tex. App.—San Antonio 2004, no pet.) (citing *Ridge Oil Co. v. Guinn Invs., Inc.*, 148 S.W.3d 143, 161–62 (Tex. 2004)). Texas courts have made it clear that “[u]nreasonable fees cannot be awarded, even if the court believes them just, but the court may conclude that it is not equitable or just to award even reasonable and necessary fees.” *Id.* The Rules of Professional Conduct set forth parameters to determine whether attorney's fees are reasonable and necessary to justify awarding the amount of fees, which include: (1) the labor and time required; (2) the likelihood that acceptance of a matter will limit available time that can be spent on other matters; (3) the usual fee charged in the surrounding community; (4) the monetary amount involved in the matter; (5) any time limitations that may be imposed; (6) the professional relationship's length and nature; (7) the experience and reputation of the lawyer; (8) and whether the matter is based on a fixed or contingent fee. TEX. DISCIPLINARY RULES PROF'L CONDUCT R. 1.04(b), reprinted in TEX. GOV'T CODE ANN., tit. 2, subtit. G, app. A (West 2005) (Tex. State Bar R. art. X, § 9); see *Hachar*, 153 S.W.3d at 142. Therefore, a two-part test first determines whether to award attorney's fees, and second determines the amount of attorney's fees to award. The first part of the test is a legal determination decided by the court, and the second part of the test is a factual finding for a jury to determine. See *Grey v. First Nat'l Bank*, 393 F.2d 371, 387 (5th Cir. 1968) (promulgating that the determination of whether the trustee acted reasonably and in good faith was a matter for the court to decide by providing that “[w]e have stated that the jury found no breach of the bank's fiduciary duties and thus we may assume that First National as trustee of the O'Connor Trust was acting reasonably and in good faith”). As a result, the scope of this Comment focuses on the court's determinations as to questions of law and not on jury determinations as to questions of fact. See *Lesikar v. Moon*, 237 S.W.3d 361, 375 (Tex. App.—Houston [14th Dist.] 2007, pet. denied) (reiterating that “[u]nder both the Declaratory Judgments Act and the Texas [Trust] Code, the trial court may award reasonable and necessary attorney fees as are equitable and just” and that “reasonable and necessary are fact questions to be determined by the fact finder” (citing TEX. CIV. PRAC. & REM. CODE ANN. § 37.009 (West 2008); *Ridge Oil*, 148 S.W.3d at 161)).

65. *Mitchell v. Mitchell*, 151 Tex. 1, 244 S.W.2d 803 (1951).

66. *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.).

“reasonably and in good faith” test results in inequities for beneficiaries. *Biggs* arose “from a decree which authorize[d] the trustees of the Aurelia Mitchell Trust to pay a fee to certain lawyers for legal services rendered by these lawyers in [*Mitchell*].”<sup>67</sup> Aurelia Mitchell created the testamentary trust in her will.<sup>68</sup> Fuhr Mitchell and Leon Mitchell, two of Aurelia’s sons, were named trustees and executors.<sup>69</sup> After the death of his mother, Leon Mitchell began acting as trustee, while Vick Mitchell replaced Fuhr Mitchell as trustee before the *Mitchell* suit was filed.<sup>70</sup> The testamentary trust created two classes of beneficiaries: life tenants and remaindermen.<sup>71</sup> The life tenants were to receive income from the trust corpus during their lives.<sup>72</sup> The remaindermen were to be paid from the trust corpus “when the life tenancies ended.”<sup>73</sup> Of note, the trustees were included in the class of life tenants.<sup>74</sup>

Trust administration problems began when the “trustees collected royalties under an oil and gas lease and on the advice of counsel treated these royalties as income under the will of Aurelia Mitchell and paid them to the life tenants.”<sup>75</sup> The exact amount of royalties paid is unknown; however, the court suggested that the evidence amounted to nearly \$100,000 in royalties.<sup>76</sup> The trust administration problems led to the remaindermen filing the initial case of *Mitchell*:

[A]s a class suit [o]n behalf of the remaindermen and in this suit it was claimed by the plaintiffs therein that the royalties which the trustees had been paying to the life tenants were not income within

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67. *Id.* at 212–13.

68. *Id.* at 213.

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.* As a reminder, the trustee is the party holding the property in trust for the beneficiary. RESTATEMENT (SECOND) OF TRUSTS § 3(3) (1959). Inherent in this role are the fiduciary duties that the trustee owes to beneficiaries of the trust. See *Grey v. First Nat'l Bank*, 393 F.2d 371, 374–76 (5th Cir. 1968) (investigating a possible breach of the fiduciary obligation that exists between the trustee and beneficiary regarding an irrevocable testamentary trust).

74. *Biggs*, 274 S.W.2d at 213

75. *Id.*

76. *Id.*

the meaning of Aurelia Mitchell's will but, under a proper construction of that will were a part of the principal of the estate and should be paid eventually to the remaindermen.<sup>77</sup>

The remaindermen sued the trustees individually and in their capacity as trustees, claiming misappropriation of the royalty funds.<sup>78</sup> More specifically, the remaindermen asked for compliance with the terms of the trust.<sup>79</sup> The plaintiffs did not explicitly plead for construction of the will and trust; however, language from counsel and the Texas Supreme Court indicate construing the will and trust was a vital part of the proceedings.<sup>80</sup> The Texas Supreme Court declared that the royalties were part of trust corpus and not income to be dispersed to life tenants, which reflected that the trustees were administering the trust improperly.<sup>81</sup> The court's holding of wrongful administration of the trust also resulted in the appointment of American National Bank of Beaumont as co-trustee with Vick and Leon Mitchell.<sup>82</sup> Once the supreme court decided *Mitchell*, counsel for the trustees filed a motion seeking "an order allowing them reasonable fees for their services to the trustees Leon Mitchell and Vick Mitchell and directing the trustees to pay this fee out of the funds of said estate."<sup>83</sup> The motion was granted and allowed for fees to be paid out of trust principal.<sup>84</sup>

The motion determination then resulted in the *Biggs* litigation.<sup>85</sup> The trial court rendered the decree for attorney's fees valid and "provided further that this fee should be paid from the

77. *Id.*

78. *Id.*

79. *Id.*

80. See *Mitchell v. Mitchell*, 151 Tex. 1, 244 S.W.2d 803, 805-07 (1951) (discussing at length the provisions of the will and the testator's intent); *Biggs*, 274 S.W.2d at 214 (implying that the Texas Supreme Court concluded that the matter was a construction issue while the appellate court made an inference that the evidence "necessarily show[s]" that the remaindermen asked that the will be construed). *But see Biggs*, 274 S.W.2d at 217 (stating that construction was not "the main object of the petition").

81. *Mitchell*, 244 S.W.2d at 807-08; see *Biggs*, 274 S.W.2d at 214 (reiterating the conclusion in *Mitchell*).

82. *Biggs*, 274 S.W.2d at 214.

83. *Id.* at 215 (internal quotation marks omitted).

84. See *id.* (explaining that one attorney was to be paid \$1,500 while the other was to receive 10% from the oil and gas lease royalties which was trust principal).

85. See *id.* ("The American National Bank, after the [motion for attorney's fees], filed the suit which is now under review.").



principal of the trust estate.”<sup>86</sup> This decision was appealed and brought before the appellate court the issue of whether attorney’s fees incurred by a trustee, who acted incorrectly in administration of the trust, could be reimbursed from the trust corpus.<sup>87</sup>

The first argument against the granting of attorney’s fees was that the attorney’s services were not used to benefit the estate, and the position of the trustees was antagonistic to the trust.<sup>88</sup> However, the court adopted the position that construction of an ambiguous trust document benefits the trust estate; therefore, charging attorney’s fees out of trust principal was proper.<sup>89</sup> However, as noted earlier, *Mitchell* was not simply a suit for construction.<sup>90</sup> The matter involved questionable trustee conduct, diversion of funds to the trustees, and depletion of a common fund.<sup>91</sup> Subsequently, “[a]ll these circumstances must be considered, in addition to the prayer for construction, in determining whether the trustees were entitled to an attorney’s fee [from the trust principal].”<sup>92</sup> Ultimately, and of significant importance, the court determined that the construction of the will was not “the main object of the petition,” but rather recovery of property.<sup>93</sup> Therefore, the court stated because the suit was not a construction action, “this rule of decision [is not] applicable to this case.”<sup>94</sup>

The second argument against the granting of attorney’s fees was “that payment out of the principal would be one by them alone, out of [the beneficiaries’] own property after their successful contest with the trustees[,] and their argument emphasizes the *supposed* injustice of this.”<sup>95</sup> The significance of *Biggs* is embodied in this second argument. Stated more clearly, “[i]t is unjust . . . that you won the suit and established [oil and gas lease]

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86. *Id.* at 216.

87. *See id.* (“The decree provided further that this fee should be paid from the principal of the trust estate. From this judgment the plaintiff bank and certain beneficiaries of the trust estate who are described as contingent beneficiaries (that is, remaindermen) have taken this appeal.”).

88. *Id.*

89. *Id.*

90. *See id.* at 217 (stressing construction was not “the main object of the petition”).

91. *Id.*

92. *Id.*

93. *Id.*

94. *Id.*

95. *Id.* at 219 (emphasis added).

royalties as corpus, but you must pay the fees out of your corpus for those who would have dissipated it.”<sup>96</sup> The beneficiaries win by being awarded royalties, but the beneficiaries lose because the funds become dissipated by paying the wrongdoer’s attorney’s fees. However, the court, citing cases outside of Texas and within, was not persuaded.<sup>97</sup> The court stated that “[g]ood faith of the representative, and necessarily the reasonableness of the action under the circumstances, have been given weight by Texas courts in situations where there was a basic duty which the representative’s good faith pulled into action in a particular suit against particular people.”<sup>98</sup> The court continued: “It seems to us that the trustees Leon Mitchell and Vick Mitchell were under a duty concerning the administration of the trust and that . . . their good faith and reasonable grounds brought this duty into operation against the remaindermen.”<sup>99</sup> Finally, after analyzing the trustees’ actions, the court deemed the trustees’ conduct reasonable and in good faith; thus, payment of attorney’s fees out of trust principal was allowed, even though the trustees administered the trust erroneously.<sup>100</sup>

*B. Codification of Sections 114.063 and 114.064 and Their Interplay with the Good Faith and Reasonableness Test*

Prior to 1985, multiple Texas cases opined on the issue of whether a trustee could be reimbursed from trust principal for attorney’s fees incurred during litigation that charged the trustee with breach of fiduciary duty or breach of trust.<sup>101</sup> For example,

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96. *Id.* (internal quotation marks omitted).

97. *Id.*

98. *Id.* at 220.

99. *Id.* at 220–21.

100. *Id.* at 220; accord SHARON B. GARDNER, TRUSTEE’S DUTIES AND OBLIGATIONS: PRACTICAL PROBLEMS, at N-27 (2007), available at [http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cts=1331750306638&ved=0CC4QFjAA&url=http%3A%2F%2Ftexasguardianship.com%2Fdocuments%2FSTCL-TrusteesDutiesandObligationsPracticalProblems.DOC&ei=o-VgT-q6Feqw2QXk-diiDCA&usg=AFQjCNHrP4\\_X9B3V1-OURdOkIzE8ZE\\_52Q](http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cts=1331750306638&ved=0CC4QFjAA&url=http%3A%2F%2Ftexasguardianship.com%2Fdocuments%2FSTCL-TrusteesDutiesandObligationsPracticalProblems.DOC&ei=o-VgT-q6Feqw2QXk-diiDCA&usg=AFQjCNHrP4_X9B3V1-OURdOkIzE8ZE_52Q) (select the “Ok” button when the download window appears) (analyzing the holding in *Biggs* as meaning that “trustees who act reasonably and in good faith in defending their actions are entitle[d] to have their attorneys’ fees paid out of the trust, even if they are found to have breached their trust”).

101. See *Van Hoose v. Moore*, 441 S.W.2d 597, 619 (Tex. Civ. App.—Amarillo 1969, writ ref’d n.r.e.) (deciding that the Texas Trust Act does not authorize recovery of

in *Grey v. First National Bank*,<sup>102</sup> trust beneficiaries alleged that a bank-trustee acquired trust property fraudulently for its own use.<sup>103</sup> The jury concluded that the trustee did not conceal material facts from the beneficiaries; thus, the trustee did not fail to comply with its fiduciary duties.<sup>104</sup> On appeal, the appellate court determined that “a trustee may charge his trust for attorney’s fees which the trustee, acting reasonably and in good faith, incurs in defense of litigation charging him with a breach of trust.”<sup>105</sup> In *duPont v. Southern National Bank of Houston*,<sup>106</sup> the court, faced with another complex trust matter, reiterated that “[g]enerally, a trustee is entitled to reimbursement from the trust estate for expenses ‘which the trustee, acting reasonably and in good faith, incurs in defense of litigation, charging him with a breach of trust.’”<sup>107</sup> Likewise, the Texas Supreme Court stated in *West Texas Bank & Trust Co. v. Matlock*<sup>108</sup> that “trustees should be allowed to pay out of the trust fund all expenses of litigation concerning such fund, in the event the litigation is forced upon them.”<sup>109</sup>

In 1985, section 114.063 of the Texas Trust Code was codified, stating that a trustee may discharge or “reimburse himself from trust principal or income or partly from both for: (1) advances made for the convenience, benefit, or protection of the trust or its property [and], (2) expenses incurred while administering or protecting the trust or because of the trustee’s holding or owning

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attorney’s fees by either party because there was no statute that addressed the issue, nor any contract between the parties that allowed for recovery); *see also* *Rowe v. Dyess*, 213 S.W. 234, 236 (Tex. 1919) (“The propriety of defending a suit or proceeding against an estate must depend upon the apparent justice of the case; and, where an administrator acts in good faith, he will not necessarily be deprived of attorneys’ fees, even though he be mistaken as to the justice of the case.”).

102. *Grey v. First Nat’l Bank*, 393 F.2d 371 (5th Cir. 1968).

103. *Id.* at 380.

104. *Id.*

105. *Id.* at 387; *accord* SHARON B. GARDNER, TRUSTEE’S DUTIES AND OBLIGATIONS: PRACTICAL PROBLEMS, at N-27 (2007) (stressing *Grey* to mean “trustees who act reasonably and in good faith in defending their actions are entitle[d] to have their attorneys’ fees paid out of the trust, even if they are found to have breached their trust”).

106. *duPont v. S. Nat’l Bank of Hous.*, 771 F.2d 874 (5th Cir. 1985).

107. *Id.* at 886 (quoting *Grey*, 393 F.2d at 387); *see* SHARON B. GARDNER, TRUSTEE’S DUTIES AND OBLIGATIONS: PRACTICAL PROBLEMS, at N-27 (2007) (reiterating the premise established in *Grey*).

108. *W. Tex. Bank & Trust Co. v. Matlock*, 212 S.W. 937 (Tex. 1919).

109. *Id.* at 941.

any of the trust property.”<sup>110</sup> This section—often referred to as the General Right to Reimbursement Statute—establishes the trustee’s general right to reimbursement because the trustee holds trust property.<sup>111</sup> Narrowing the general right of reimbursement to the issue of attorney’s fees and costs, section 114.064, also codified in 1985, provides that “[i]n any proceeding under this code, the court may make such award of costs and reasonable and necessary attorney’s fees as may seem equitable and just.”<sup>112</sup>

Texas courts analyzing sections 114.063 and 114.064 have opined that “[t]he Texas Trust Code authorizes the reimbursement of a trustee from trust principal or income and specifically provides for awards of attorney’s fees.”<sup>113</sup> *Combs v. Gent*<sup>114</sup> echoed section 114.064 by quoting its language verbatim in the court’s opinion regarding whether the trustee involved was entitled to attorney’s fees.<sup>115</sup> In *Lyc0 Acquisition 1984 Ltd. v. First National Bank of Amarillo*<sup>116</sup> and *Hachar v. Hachar*,<sup>117</sup> both courts acknowledged that the award of attorney’s fees is “within the sound discretion of the trial court.”<sup>118</sup>

However, when a matter in litigation concerns whether a trustee can recover attorney’s fees from trust funds for defending an action brought by a beneficiary, the codification of sections 114.063 and 114.064 has not stopped Texas courts from applying the pre-1985 test of acting “reasonably and in good faith.”<sup>119</sup> The interplay between case law and sections 114.063 and 114.064 has resulted in convoluted and inconsistent judicial tests. For example, in November 2000, the Texas Thirteenth Court of Appeals in *Stone v. King*<sup>120</sup> held that “Stone breached his fiduciary duties by failing to distribute trust funds after being

110. TEX. PROP. CODE ANN. § 114.063 (West 2007).

111. *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*4 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication).

112. PROP. § 114.064 (West 2007).

113. *Moody*, 1999 WL 1041541, at \*4.

114. *Combs v. Gent*, 181 S.W.3d 378 (Tex. App.—Dallas 2005, no pet.).

115. *Id.* at 385–86.

116. *Lyc0 Acquisition 1984 Ltd. v. First Nat’l Bank of Amarillo*, 860 S.W.2d 117 (Tex. App.—Amarillo 1993, writ denied).

117. *Hachar v. Hachar*, 153 S.W.3d 138 (Tex. App.—San Antonio 2004, no pet.).

118. *Id.* at 142; *Lyc0 Acquisition*, 860 S.W.2d at 121.

119. *Grey v. First Nat’l Bank*, 393 F.2d 371, 387 (5th Cir. 1968).

120. *Stone v. King*, No. 13-98-022-CV, 2000 WL 35729200 (Tex. App.—Corpus Christi Nov. 30, 2000, pet. denied) (not designated for publication).

directed to do so by King's attorney and by adding D'Unger as a signatory to the trust account."<sup>121</sup> The court then applied the test established prior to 1985 by stating that "a trustee may charge the trust for attorney's fees that the trustee, acting reasonably and in good faith, incurs defending charges of breach of trust," instead of applying the appropriate test of "equitable and just" found in section 114.064.<sup>122</sup>

*Moody Foundation v. Estate of Moody*,<sup>123</sup> decided in 1999, also illustrates the interplay between case law and the codified statutes.<sup>124</sup> Presumably, the equitable-and-just test of section 114.064 applied to the litigation.<sup>125</sup> However, despite the majority's discussion of the applicability of the Trust Code and section 114.064, the court proceeded to utilize the good faith and reasonableness test.<sup>126</sup> The court explained that under Texas case law, a trustee has a right to charge the trust attorney's fees, incurred in litigation regarding the trustee's breach of fiduciary duty if the trustee is acting reasonably and in good faith.<sup>127</sup>

Further proving inconsistent application of the test, in *Caldwell v. River Oaks Trust Co.*,<sup>128</sup> the appellate court carefully analyzed whether a trustee may charge the trust for attorney's fees by utilizing section 114.063 combined with the good faith and reasonableness test.<sup>129</sup> Although the court properly referenced section 114.063, the court failed to consider application of the correct statute, section 114.064.<sup>130</sup>

The interplay of Texas case law and sections 114.063 and 114.064 creates more questions than answers. Presumably, the

121. *Id.* at \*8.

122. *Id.*

123. *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication).

124. *See id.* at \*4–5 (explaining the application of section 114.064 to the facts of the case, but ultimately relying on the good faith and reasonableness test for determining that the trustee may recover attorney's fees from the trust).

125. *See* TEX. PROP. CODE ANN. § 114.064 (West 2007) (regarding the award of attorney's fees under the equitable-and-just test); *Moody*, 1999 WL 1041541, at \*4 (indicating section 114.064 controls a trustee's reimbursement of attorney's fees from the trust).

126. *Moody*, 1999 WL 1041541, at \*4–5.

127. *Id.* at \*5.

128. *Caldwell v. River Oaks Trust Co.*, No. 01-94-00273-CV, 1996 WL 227520 (Tex. App.—Houston [1st Dist.] May 2, 1996, writ denied) (not designated for publication).

129. *Id.* at \*18.

130. *See id.* at \*17–18 (making no reference to Trust Code section 114.064).

tests work together, and the equitable-and-just test of section 114.064 is satisfied if the trustee acted reasonably and in good faith.<sup>131</sup> However, as illustrated above, most courts only apply one test and not both, nullifying the proposition that both tests work concurrently.<sup>132</sup>

### C. Sections 114.063 and 114.064 and Their Failure to Prevent Inequity

In 2004, after codification of sections 114.063 and 114.064, the Texas Fourth Court of Appeals decided *Hachar v. Hachar*.<sup>133</sup> “After reviewing a complex factual background, the trial court awarded attorney’s fees from the trust in favor of both the trustee and the beneficiaries who were involved in litigation against each other.”<sup>134</sup> The beneficiaries argued against the award of attorney’s fees from the trust principal in favor of the trustees because the trustees were not the prevailing party.<sup>135</sup> In fact, the beneficiaries were successful in having the trustee removed and replaced.<sup>136</sup> However, the appellate court held that “the trial

131. Compare TEX. PROP. CODE ANN. § 114.064 (West 2007) (“In any proceeding under this code the court may make such award of costs and reasonable and necessary attorney’s fees as may seem equitable and just.”), with *Grey v. First Nat’l Bank*, 393 F.2d 371, 387 (5th Cir. 1968) (begging the question that if one acts reasonably and in good faith, would the award of attorney’s fees be equitable and just).

132. See *Combs v. Gent*, 181 S.W.3d 378, 385–86 (Tex. App.—Dallas 2005, no pet.) (applying only section 114.064); *Hachar v. Hachar*, 153 S.W.3d 138, 142–45 (Tex. App.—San Antonio 2004, no pet.) (employing section 114.064 but not the good faith and reasonableness test); see also *Moody*, 1999 WL 1041541, at \*5 (discussing section 114.064’s applicability but only applying the good faith and reasonableness test to the trustee’s misconduct); *Lycos Acquisition 1984 Ltd. v. First Nat’l Bank of Amarillo*, 860 S.W.2d 117, 120–22 (Tex. App.—Amarillo 1993, writ denied) (refusing to apply the test found in *Grey* and only applying section 114.064).

133. See *Hachar*, 153 S.W.3d at 142 (utilizing section 114.064).

134. Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006); see *Hachar*, 153 S.W.3d at 143 (affirming the trial court’s award of attorney’s fees based on the premise that section 114.064 is not dependent on a party substantially prevailing).

135. Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006); see *Hachar*, 153 S.W.3d at 143 (arguing that attorney’s fees should only be awarded to the prevailing party).

136. See *Hachar*, 153 S.W.3d at 143 (stating that the beneficiaries believed they were the prevailing party since they succeeded in “removing the development and management of the trust’s land from [the trustee’s] control”). The original suit was commenced because the beneficiaries alleged that the trustee “had violated the terms of the trust and breached his fiduciary duty in the manner in which he managed the trust property.” *Id.* at 141. Therefore, the beneficiaries’ belief that they were successful in the suit was well-founded.

court could make the award [of attorney's fees in favor of the trustee] because Trust Code [s]ection 114.064 permitted the court to make an award that was 'equitable and just.'"<sup>137</sup> The holding shows that section 114.064 fails to achieve equity by allowing an award of attorney's fees from trust funds even though the trustee acted wrongfully and was removed.<sup>138</sup>

Section 114.064's weakness in equity causes beneficiaries to lose even when they win.<sup>139</sup> In turn, one commentator has explained that *Hachar*:

[R]eminds litigants that any party involved in trust litigation should seek an award of attorney's fees under Trust Code [s]ection 114.064 because the court has the authority to award fees even in favor of the losing party if the court believes that it is equitable and just to make such an award.<sup>140</sup>

Not only did *Hachar* show that application of sections 114.063 and 114.064 can yield unjust results, but it reminds us that the issue was prevalent before their codification.

#### D. *Recognition of the Inequity for Winning Beneficiaries*

The court recognized in *Biggs* the injustice of awarding a negligent trustee attorney's fees from the trust even though a

137. Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (quoting *Hachar*, 153 S.W.3d at 142).

138. See TEX. PROP. CODE ANN. § 114.064 (West 2007) (attempting to achieve equity by utilizing a test based on equitable considerations; however, equity is not reached in factual situations); see also SHARON B. GARDNER TRUSTEE'S DUTIES AND OBLIGATIONS: PRACTICAL PROBLEMS, at N-27 (2007), available at [http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cts=1331750306638&ved=0CC4QFjAA&url=http%3A%2F%2Ftexasguardianship.com%2Fdocuments%2FSTCL-TrusteesDutiesandObligationsPracticalProblems.DOC&ei=o-VgT-q6Feqw2QXk-diDCA&usg=AFQjCNHrP4\\_X9B3V1-OURdOkIzE8ZE\\_52Q](http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cts=1331750306638&ved=0CC4QFjAA&url=http%3A%2F%2Ftexasguardianship.com%2Fdocuments%2FSTCL-TrusteesDutiesandObligationsPracticalProblems.DOC&ei=o-VgT-q6Feqw2QXk-diDCA&usg=AFQjCNHrP4_X9B3V1-OURdOkIzE8ZE_52Q) (select the "Ok" button when the download window appears) (analyzing Texas case law as allowing trustees to be awarded attorney's fees even though the trustee is found to have breached trust).

139. See generally *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 219 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (expressing the notion that when a beneficiary is successful in a suit against a trustee, but attorney's fees nonetheless are awarded to the trustee from trust funds, the beneficiaries in fact lose when they win). The court stated that "[i]t is unjust . . . that you won the suit and established royalties as corpus, but you must pay the [wrongdoer's attorney's] fees out of your corpus . . ." *Id.* (internal quotation marks omitted).

140. Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006).

beneficiary “won the suit.”<sup>141</sup> In analyzing the situation, the court considered language found in *In re Drake's Will*.<sup>142</sup>

In effect it amounts to this: That a beneficiary, who has cause to have the account of his trustee surcharged in a substantial amount, can be called upon by the trustee to face the prospect that, if he wants to litigate the question of the trustee's liability, he will have to pay not only his own but the trustee's attorneys' fees and the trustee's fees for contesting the claim, even if the beneficiary succeeds in the action.<sup>143</sup>

The court in *Biggs* further reflected on *Melson v. Travis*,<sup>144</sup> which similarly represented:

[I]f [the trustee] *mismanages or misappropriates* the trust estate, and the beneficiaries have to bring an action against him on account thereof, he is not entitled to charge the trust estate with the fees for defending his own maladministration against the complaint of the beneficiaries. To permit him to do so would be to allow a trustee fees out of the estate, not for defending it, but for defending against it.<sup>145</sup>

Additionally, in *Biggs*, the court identified cases “which have allowed the trustee his expense although his view was erroneous, his action unsuccessful, and his conduct the cause of the litigation from which the expense resulted.”<sup>146</sup> Specifically, the court referenced *In re Sellers' Estate*,<sup>147</sup> in which the court did not base its reasoning upon the fault of the trustee, but instead on the reasonableness of the trustee's actions.<sup>148</sup>

In consideration of the above cases, Texas courts have set forth a good faith and reasonableness test that the courts still follow, along with the similar test found in section 114.064.<sup>149</sup> The

141. See *Biggs*, 274 S.W.2d at 219 (pointing out the “supposed” injustice).

142. *In re Drake's Will*, 263 N.W. 439 (Minn. 1935).

143. *Id.* at 442; see *Biggs*, 274 S.W.2d at 219 (relying upon *In re Drake's Will* in the analysis).

144. *Melson v. Travis*, 66 S.E. 936 (Ga. 1910).

145. *Id.* at 937 (emphasis added); accord *Biggs*, 274 S.W.2d at 219 (relying upon *Melson*).

146. *Biggs*, 274 S.W.2d at 219.

147. *In re Sellers' Estate*, 67 A.2d 860 (Del. Ch. 1949).

148. *Id.* at 874; see *Biggs*, 274 S.W.2d at 219 (directing attention to *In re Sellers' Estate*).

149. See, e.g., *Stone v. King*, No. 13-98-022-CV, 2000 WL 35729200, at \*8 (Tex. App.—Corpus Christi Nov. 30, 2000, pet. denied) (not designated for publication)



interplay between the two tests clearly has potential to result in the inequity of a successful litigant being penalized through payment of the wrongdoer's attorney's fees.<sup>150</sup>

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(permitting the continued use of the reasonableness test even after codification of section 114.064).

150. See *Biggs*, 274 S.W.2d at 219 (highlighting the "supposed" injustice). Another potential inequity of the current interplay is that Texas courts work under the assumption that the trust has sufficient funds to pay the awarded attorney's fees. See *id.* at 222 (awarding attorney's fees from trust principal, indicating that the court must make the assumption that there are sufficient funds in the trust to pay attorney's fees when awarding attorney's fees from the trust principal). The assumption could result in unfair and unjust decisions. For example, each trustee of trusts *A* and *B* breach a fiduciary duty by improperly investing trust funds pursuant to the prudent investors rule. See TEX. PROP. CODE ANN. § 113.006 (West 2007) (laying out the general authority to invest and manage trust property by stating, "a trustee may manage the trust property and invest and reinvest in property of any character on the conditions and for the lengths of time as the trustee considers proper, notwithstanding that the time may extend beyond the term of the trust"). *A* has assets worth \$100,000 while *B* has assets of \$1,000,000. The beneficiaries of trusts *A* and *B* both bring suit against their respective trustees for breach of their fiduciary duties. See *Midland Shoe Co. v. A.L. & K. Dry Goods Co.*, 3 S.W.2d 475, 478 (Tex. Civ. App.—Amarillo 1927, writ ref'd) (explaining that trust beneficiaries have standing to sue the trustee). Both trustees defend their misconduct. See *City of Austin v. Cahill*, 88 S.W. 542, 554 (Tex. 1905) (Padelford, J., concurring) ("Whenever a person has the possession, title, and management of property or funds for the benefit of others . . . such trustee or quasi trustee can institute and prosecute, or defend, suits affecting such property or funds . . ." (emphasis added)). However, based on the interplay between case law and sections 114.063 and 114.064, judges in both cases deem that, although the trustees breached their fiduciary duties and caused \$75,000 in damages, an award of attorney's fees would be equitable and just; thus, both judges allow attorney's fees to be awarded out of the trusts. See *Hachar v. Hachar*, 153 S.W.3d 138, 141 (Tex. App.—San Antonio 2004, no pet.) (concurring with the trial court's decision to award attorney's fees based on the equitable-and-just test even though the trustee did not prevail). The interplay being equally applied in both situations works under the assumption that both trusts have sufficient funds to reimburse incurred attorney's fees. See *id.* (assuming that the trust has sufficient funds to pay the awarded attorney's fees). If the attorney's fees are \$100,000 for the trustees, trust *A* would be repaid \$75,000 in losses incurred by the trustee, bringing the trust's value back to \$100,000; however, payment of the \$100,000 in attorney's fees would completely deplete the trust. See PROP. § 114.001(c) (West 2007) ("A trustee who commits a breach of trust is chargeable with any damages resulting from such breach of trust."); RESTATEMENT (SECOND) OF TRUSTS § 205 (1959) (concurring that a trustee is "chargeable with . . . any loss . . . in value of the trust estate resulting from the breach of the trust"). The result for the *winning* beneficiary of trust *A* is a *loss* of 100% of the trust. However, trust *B* would be depleted to \$900,000 after attorney's fees and reimbursement, resulting in a loss of \$100,000, but only a 10% loss of the value of the trust. The assumption creates a myriad of questions because of the disparate treatment and overwhelming discrimination served on smaller trusts. Is the result of the rule equitable? See *generally* PROP. § 114.064 (West 2007) (evidencing the intent to provide a rule that is equitable by use of the phrase "equitable and just"). Could a court utilizing the good faith and reasonableness test or the equitable-and-just test find that attorney's fees in trust *A*'s situation are not equitable and just or reasonable because the fees deplete the trust? How

#### IV. WHY THE CURRENT INTERPLAY MATTERS AND MUST BE CHANGED

##### A. *The Interplay Provides No Incentive for Trustees to Act in Accordance with Their Fiduciary Duties*

The interplay between case law and Texas Trust Code sections 114.063 and 114.064 offers little incentive for a beneficiary to bring suit against a trustee to compel compliance with its fiduciary duties.<sup>151</sup> A basic premise of law is that laws provide

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would the court subsequently award a fee? If the fee is reduced, however, the attorney for the trustee of trust *A* gets paid less than the attorney for trustee of trust *B* for the same work performed. This assumption has not been recognized in Texas courts and is similar to another contradiction in trust litigation. See Frank N. Ikard, Jr., TRUST LITIGATION IN TEXAS, 10 (2004), available at [http://igjlaw.com/frank\\_ikard\\_articles/trust\\_litigation\\_in\\_texas.pdf](http://igjlaw.com/frank_ikard_articles/trust_litigation_in_texas.pdf) (introducing an inherent paradox in fiduciary litigation). This paradox that largely is unrecognized by Texas courts involves “the trustee, who is usually defending himself out of the trust estate (which belongs more to the beneficiary rather than to the trustee) and the beneficiary who is usually attempting to prosecute the cause of action against the trustee with his own resources.” *Id.* The trustee then “of course” utilizes sections 114.063 and 114.064 to charge all fees and costs to the beneficiary’s trust. *Id.* The paradox becomes apparent when the beneficiary is also the person who created the trust, known as the settlor, and the beneficiary brings suit against the trustee to dispute the validity of the trust. See RESTATEMENT (SECOND) OF TRUSTS § 3(1) (1959) (defining the settlor as the person who creates the trust). See generally *Fewell v. Republic Nat’l Bank of Dall.*, 513 S.W.2d 596, 598 (Tex. Civ. App.—Eastland 1974, writ ref’d n.r.e.) (acknowledging that one reason why a settlor–beneficiary would want to revoke a trust is that the trust’s purpose can no longer be accomplished). If the beneficiary’s attack on the validity of the trust is successful, as a result, there is no trust and nothing for the attorney to recover from, yet the trustee has been charging fees to it. Frank N. Ikard, Jr., TRUST LITIGATION IN TEXAS, 119 (2004). Because “[t]his paradox is not recognized (or if recognized, not given much credence) by most Texas judges,” Texas courts have failed to recognize a parallel paradox regarding attorney’s fees in trust litigation. *Id.* at 10.

151. See Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. Rev. 1603, 1643 (2006) (concluding that the end result of *Hachar* is that it reminds unsuccessful litigants to seek an award of attorney’s fees under section 114.064). Awarding fees to the losing party discourages a beneficiary from bringing a suit against a trustee because even if the beneficiary wins the suit, the trustee is likely going to be awarded attorney’s fees out of the trust. See *id.* (pointing out that a losing party can still win). From a purely economic standpoint, rarely will the benefits of recovery outweigh the costs incurred in pursuit of recovery. For example, a trust has assets of \$1,000,000. Through the trustee’s negligence, the value of the assets drops 25% to \$750,000. In defending a suit brought by a trust beneficiary, the trustee’s attorney’s fees are approximately \$200,000. See generally CHARLES M. HORNBERGER, ATTORNEY’S FEES IN TRUST AND ESTATE LITIGATION 15 (2011), available at <http://www.stmarytx.edu/law/pdf/CLEAttorneysFees.pdf> (providing a thorough analysis of litigation costs in contested trust matters by breaking down the costs of research, discovery, motions, experts, and more). If the beneficiary establishes a breach of fiduciary duty claim, but the court allows attorney’s fees awarded out of trust corpus, the net result after litigation would be that the trust corpus is valued at \$550,000, a 45%

incentives for the ways in which people should act.<sup>152</sup> The best example of the role these incentives play in the legal profession is illustrated in the Texas Lawyer's Creed, which was promulgated by the Texas Court of Criminal Appeals and the Texas Supreme Court.<sup>153</sup> The Creed states: "The desire for respect and confidence by lawyers from the public should provide the members of our profession with the necessary incentive to attain the highest degree of ethical and professional conduct."<sup>154</sup>

As the incentives of respect and confidence are the necessary force for lawyers to achieve exceptional professional and ethical obedience, the logic also rings true that laws should act as the necessary incentive for compliance with civil standards.<sup>155</sup> For instance, the Texas Trust Code provides that "[a] trustee who commits a breach of trust is chargeable with any damages resulting from such breach of trust."<sup>156</sup> Trustees are incentivized to not breach their fiduciary duty because if a trustee breaches the duty, the trustee becomes liable for damages to the beneficiary.<sup>157</sup> Also, if a trustee breaches a fiduciary duty, the trustee is required

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loss. However, the trustee would be required to return the \$250,000 to make the beneficiary whole as a result of the breach. See PROP. § 114.001(c) ("A trustee who commits a breach of trust is chargeable with any damages resulting from such breach of trust . . ."). This would bring the trust corpus back to \$800,000, resulting in a *loss* of \$200,000, or 20%, for the *winning* beneficiary. The lack of an incentive to sue is also true for smaller trusts; in fact, smaller trusts realize an even bigger incentive *not* to sue. The gloomy economics provide little incentive for a wronged beneficiary to right the malfeasance.

152. See *Stassi v. Boone*, No. GN200180, 2003 WL 21436995, at \*17 (Tex. Dist. Ct. June 6, 2003) (not designated for publication) ("The common[-]benefit doctrine provides an incentive . . ." (quoting *In re Pub. Serv. Co. of New Mexico*, No. 91-0536M, 1992 WL 278452, at \*3 (S.D. Cal. Jul. 28, 1992)) (internal quotation mark omitted)); see also *Robinson v. Brice*, 894 S.W.2d 525, 528 (Tex. App.—Austin 1995, writ denied) ("[T]he prejudgment[-]interest statute provides a series of incentives designed to encourage the expeditious settlement of claims.").

153. See SUPREME COURT OF TEX. & COURT OF CRIMINAL APPEALS, THE TEXAS LAWYER'S CREED—A MANDATE FOR PROFESSIONALISM (1989), available at <http://www.supreme.courts.state.tx.us/pdf/TexasLawyersCreed.pdf> (outlining elements of professionalism).

154. *Delta Air Lines, Inc. v. Cooke*, 908 S.W.2d 632, 635 (Tex. App.—Waco 1995, no writ) (quoting SUPREME COURT OF TEX. & COURT OF CRIMINAL APPEALS, THE TEXAS LAWYER'S CREED—A MANDATE FOR PROFESSIONALISM (1989)).

155. See *id.* (deciding that respect and confidence from the public should act as incentives for attorneys to act ethically, which in turn parallels the ideology that laws should incentivize the masses to act prudently).

156. PROP. § 114.001(c).

157. See *id.* (asserting a strong incentive to not breach a duty owed to a beneficiary).

to forfeit its trustee's fee, and case law allows for punitive damages in certain circumstances.<sup>158</sup> Laws defining the expectations of trustees regarding their fiduciary duties were established to incentivize trustees to act in accordance with their position of inherent power.<sup>159</sup>

The Texas Trust Code provides that if these laws fail to incentivize a rogue trustee, then that trustee must make the wronged beneficiary whole by rectifying "any loss or depreciation in value of the trust estate as a result of the breach of trust; . . . any profit made by the trustee through the breach of trust; . . . or any profit that would have accrued to the trust estate if there had been no breach of trust."<sup>160</sup> However, sections 114.063 and 114.064, along with accompanying case law, fail to present a clear incentive for trustees to act in accordance with their fiduciary duties and to make the wronged beneficiary whole.<sup>161</sup> The interplay allows a

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158. See *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 160 S.W.2d 509, 514 (Tex. 1942) (calling for fee forfeiture); see also *Hawthorne v. Guenther*, 917 S.W.2d 924, 936 (Tex. App.—Beaumont 1996, writ denied) (allowing for punitive damages in the correct circumstances).

159. See *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928) (detailing the strict obligations of a fiduciary and explaining that the duties placed on fiduciaries are present because of the inherent power they possess).

160. PROP. § 114.001(c).

161. See *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 219 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (discussing the unjustness of telling a prevailing remainderman in an oil and gas lawsuit "you must pay the fees out of your corpus for those who would have dissipated it," but still awarding attorney's fees from the trust corpus to trustees who acted wrongfully); see also Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (identifying *Hachar* as encouraging unsuccessful litigants to pursue an award of attorney's fees). The net result of these cases, one using section 114.064 and the other using the good faith and reasonableness test, is the trustee who fails to act in accordance with his or her fiduciary duties can have one of two results. See *Hachar v. Hachar*, 153 S.W.3d 138, 142–43 (Tex. App.—San Antonio 2004, no pet.) (analyzing section 114.064); *Biggs*, 274 S.W.2d at 220–22 (finding that if the trustee acts reasonably and in good faith, an award of attorney's fees out of trust corpus is appropriate). In one scenario, the trustee could defend the suit and win, resulting in no damages owed and an award of attorney's fees—a win-win situation for the trustee. However, the trustee could lose the suit and owe damages, but if the actions were reasonable and in good faith, the trustee would likely be reimbursed for attorney's fees. See *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*4–5 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication) (examining the current law in Texas regarding section 114.064, and explaining that "[u]nder Texas law, a trustee may charge the trust for attorney's fees [that] the trustee, acting reasonably and in good faith, incurs defending charges of breach of trust"). While the thought of owing damages may incentivize a trustee to act in accordance with his or her fiduciary duties, the thought of being reimbursed for attorney's fees to defend the suit

trustee to act neglectfully but still be awarded attorney's fees.<sup>162</sup> The only fear a trustee may have is an award of damages; however, in many trust matters, this fear is negated by the fact that even damages do not necessarily result in a loss to the trustee,<sup>163</sup> as seen in case law.<sup>164</sup>

Trustees are held to the most sensitive "punctilio of an honor, . . . [which] has developed a tradition that is unbending and inveterate."<sup>165</sup> However, the current interplay between case law and sections 114.063 and 114.064 is not unbending. In fact, the interplay reduces the sensitive standard to a mere reasonableness

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provides no incentive to avoid suit. Also, in many trust cases, damages owed by the trustee are merely damages arising from the trustee personally profiting from the trust; therefore, the damages that must be repaid are assets that never rightfully belonged to the trustee in the first place. *See Slay v. Burnett Trust*, 187 S.W.2d 377, 393–94 (Tex. 1945) (writing that the beneficiary can recover for profits made by the trustee through the trustee's inappropriate use of trust funds). For example, suppose a trustee takes 50% of trust income for personal gain instead of paying the income to the beneficiaries. The trustee would owe the trust the 50% he took, which was not money the trustee ever rightfully owned; therefore, paying the money back to the trust is not an actual loss to the trustee. Consequently, trustees have little incentive through the current interplay to act in accordance with their fiduciary duties. If a duty is breached, the trustee frequently suffers no real loss, even if damages are awarded, and so long as the trustee acts reasonably, a court has full authority to reimburse attorney's fees incurred.

162. *See Grey v. First Nat'l Bank*, 393 F.2d 371, 387 (5th Cir. 1968) (indicating that attorney's fees may be assessed against the trust if the trustee's defense is reasonable and in good faith); *see also Biggs*, 274 S.W.2d at 222 (holding that equitable considerations, such as a trustee's acting reasonably and in good faith in defending his or her actions, shall be taken into account when determining "whether a trustee should be awarded an attorney's fee"). However, a trustee's actions based on a mistake of law will not necessarily grant a trustee attorney's fees; "the trustee's good faith and the reasonableness of his [or her] actions are matters to be considered." *Id.*

163. *See PROP. § 113.082(a)* (West 2007) (providing for the denial of a trustee's compensation if the trustee "materially violate[s] or attempt[s] to violate the terms of the trust and the violation or attempted violation results in a material financial loss to the trust").

164. *See Reed v. Stringer*, 472 S.W.2d 329, 331 (Tex. Civ. App.—Beaumont 1971, writ ref'd n.r.e.) (stressing that damages were levied against the trustee for his self-dealing but the trustee never realized an actual loss). The trustee sold himself shares of stock from the trust in question for \$2.00, which was improper self-dealing. *Id.* The trustee then sold the shares to an insurance company for \$8.00, at a profit of \$6.00 per share, again, which was improper. *Id.* The trustee improperly sold himself 6,000 shares and sold all of these common-stock shares for a net profit of \$36,000. *Id.* at 330–31. However, this \$36,000 was never rightfully the trustee's; thus, the court requiring the trustee to pay these funds back is not an actual loss to the trustee. The importance of this concept comes full circle considering a court may award attorney's fees for the trustee from the trust resulting in no real loss to the trustee.

165. *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928).

and equitable standard.<sup>166</sup> This unsavory reduction does not provide the incentive necessary to induce trustees to act in accordance with the unwavering duty of prudence owed to their beneficiaries.

*B. The Interplay Is Not Serving the Clear Intent of Section 114.064*

In the bill analysis for section 114.064, the Texas Senate Committee on State Affairs explained that “the current Code does not contain a provision allowing the court to award costs and attorney’s fees to a trustee *who prevails* in an action for removal or . . . surcharge.”<sup>167</sup> Absent is any language stating or implying that the purpose of the statute was to allow courts the authority to award attorney’s fees from a trust to a trustee who does not prevail.<sup>168</sup> In fact, legislative intent seems to indicate that the statute should act as a prevailing party statute, in that if the trustee prevails in a removal or surcharge action then costs and fees should be allowed from trust funds; but if the trustee does not prevail, then the trustee is not entitled to costs and fees from trust funds.<sup>169</sup> Despite the clear intent of the legislature, courts have

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166. *Id.*; accord PROP. § 114.064 (West 2007) (“In any proceeding under this code the court may make such award of costs and reasonable and necessary attorney’s fees as may seem equitable and just.”); *Biggs*, 274 S.W.2d at 220–21 (holding that an award of attorney’s fees out of trust corpus is appropriate if the trustee acts reasonably and in good faith).

167. SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985) (emphasis added).

168. *See id.* (codifying the Texas Legislature’s intent to award attorney’s fees to a trustee who prevails, omitting language stating that attorney’s fees should be awarded to a trustee who does not prevail in a removal or surcharge action).

169. *But see, e.g.*, *Barshop v. Medina Cnty. Underground Water Conservation Dist.*, 925 S.W.2d 618, 637 (Tex. 1996) (determining that the award of fees and costs is not based on which party substantially prevailed); *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*4 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication) (indicating the court does not take into consideration who prevails); *Lycos Acquisition 1984 Ltd. v. First Nat’l Bank of Amarillo*, 860 S.W.2d 117, 121 (Tex. App.—Amarillo 1993, writ denied) (stressing the determination under section 114.064 that the award of attorney fees was “within the sound discretion of the trial court”). These cases, along with other similar holdings, interpret section 114.064 as a statute that provides broad discretion to the court to seemingly dole out attorney’s fees under any circumstance that falls within the indefinable terms of “equitable and just.” *See* PROP. § 114.064 (utilizing ambiguous equitable-and-just language).

consistently held the opposite, much like in *Hachar*, that “section 114.064 is not a prevailing party statute.”<sup>170</sup>

The question is why the intent of the statute, which seems to be to award the prevailing party attorney’s fees, varies from the actual codified language.<sup>171</sup> One could argue that the differing language was to make the statute more analogous to the Texas Probate Code.<sup>172</sup> The bill analysis specifically addressed the lack of a provision in the Trust Code “allowing the court to award costs and attorney’s fees to a trustee who prevails in an action[,]” and briefly mentioned that “[t]he Texas Probate Code permits such recovery by an executor or administrator of an estate.”<sup>173</sup> However, what is vitally important to discern is that the mentioning of the Probate Code was not intended to link the Trust and Probate Codes, but rather to provide an illustration as to the necessity of the statute.<sup>174</sup> The bill analysis merely references the Probate Code as a reason for the new statute, as opposed to a guiding principle, thus rebutting any argument that the codified section 114.064 must be linked to the Texas Probate Code.<sup>175</sup>

Also, at the time Trust Code section 114.064 was codified, a multitude of cases had already analyzed Probate Code sections 149C and 245, which addressed the issue of attorney’s fees in probate matters.<sup>176</sup> Such cases that analyzed these statutes

170. *Hachar v. Hachar*, 153 S.W.3d 138, 143 (Tex. App.—San Antonio 2004, no pet.) (citing *Barshop*, 925 S.W.2d at 637).

171. See SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985) (implying the purpose of section 114.064 was to allow the award of costs and attorney’s fees to the prevailing party). *But see* PROP. § 114.064 (showing the actual codified language varies from the original intent, because it provides for attorney’s fees and costs “[i]n any proceeding under this code” as long as it is equitable and just).

172. See *id.* (indicating that a prevailing-party statute exists under the Texas Probate Code, but noting the absence of such a statute under the Trust Code).

173. *Id.*

174. See *id.* (referencing the Probate Code as a reason why a prevailing-party statute should be written into the Trust Code).

175. See *id.* (stating the intent of Trust Code section 114.064, and attempting to illustrate why a prevailing-party statute may be necessary, but not implying that Trust Code section 114.064 should be linked to the Probate Code).

176. See TEX. PROB. CODE ANN. § 149C(c) (West Supp. 2011) (“An independent executor who defends an action for his removal in good faith, whether successful or not, shall be allowed out of the estate his necessary expenses and disbursements, including reasonable attorney’s fees, in the removal proceedings.”); see also *id.* § 245 (“When a personal representative neglects to perform a required duty or if a personal representative is removed for cause the personal representative and the sureties on the personal representative’s bond are liable for: (1) costs of removal and other additional costs

were contradictory and vastly inconsistent.<sup>177</sup> Thus, the argument that the statute was designed to provide a rule more analogous to that of the Probate Code is undermined significantly, because the legislature likely would not have created a statute analogous to probate statutes that were producing convoluted and disparate results.<sup>178</sup>

Further, language parallel to Trust Code section 114.064 is nowhere present in the Probate Code. Because similar rules were not used, the legislature likely did not intend to create an analogous rule to the Probate Code.<sup>179</sup>

Additionally, an argument could be set forth that the Texas Legislature intended the statute to be a broad grant of attorney's fees for all matters properly brought under the Trust Code.<sup>180</sup>

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incurred that are not authorized expenditures, as defined by this code; and (2) reasonable attorney's fees incurred in removing the personal representative or in obtaining compliance regarding any statutory duty the personal representative has neglected.”)

177. *Compare* *Fillion v. Osborne*, 585 S.W.2d 842, 845 (Tex. Civ. App.—Houston [1st Dist.] 1979, no writ) (interpreting Probate Code section 245 “to ensure that the estate will not be charged with fees or any costs which are incurred by reason of fault of the personal representative”), *with* *Klein v. Klein*, 641 S.W.2d 387, 390 (Tex. App.—Dallas 1982, no writ) (implying that if the executor acts in good faith in defense of a suit, then the executor is required under the Probate Code to be awarded attorney's fees from the estate).

178. *See* *Lawyers Sur. Corp. v. Larson*, 869 S.W.2d 649, 652 (Tex. App.—Austin 1994, writ denied) (analyzing Probate Code sections 241 and 242 and determining that it is inequitable to charge an estate for the malfeasance of an executor). *But see* *Garcia v. Garcia*, 878 S.W.2d 678, 681 (Tex. App.—Corpus Christi 1994, no writ) (distinguishing *Lawyers Surety Corp.* by interpreting Probate Code section 149C as holding an estate can be liable for the attorney's fees of the executor and beneficiary in a removal action that is defended in good faith). The convoluted and inconsistent analysis of the Probate Code has continued after codification of Trust Code section 114.064. However, a survey of cases shows that the majority of courts concur with the sentiment echoed in *Lawyers Surety Corp.*, which stated that the costs of removal “are assessed against the administrator and the surety because of the inequities inherent in penalizing the estate for the administrator's negligence.” *Lawyers Sur. Corp.*, 869 S.W.2d at 652. The holding in *Garcia* is rarely followed, presumably because of the inherent inequity. *See* *Norman v. Finley*, No. 04-01-00394-CV, 2002 WL 341585, at \*9 (Tex. App.—San Antonio, Mar. 6, 2002) (not designated for publication) (illustrating *Garcia's* obtuse reasoning that failure to award attorney's fees implies that the trustee was “not defending in good faith”).

179. *See* TEX. PROP. CODE ANN. § 114.064 (West 2007) (awarding attorney's fees when equitable and just). Nowhere in the Probate Code is this language codified; the Probate Code sections that are generally applicable to attorney's fees in estate litigation are sections 149C and 245. *See* PROB. § 149C(c) (permitting an independent executor to pay his own necessary expenses, for a good-faith defense of his removal, from the corpus of the trust, regardless of the suit's outcome); *id.* § 245 (establishing the liability of the personal representative and the “sureties on the personal representative's bond”).

180. *See* *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*4-5 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication)



Such intent is necessary because “[i]n Texas, the well-settled law is that attorney’s fees are not recoverable in an action unless provided by statute or a contract between the parties.”<sup>181</sup> The argument follows, that the Texas Legislature may have strayed from its intent to provide attorney’s fees and costs to a prevailing trustee in more than just removal or surcharge actions.<sup>182</sup> However strong this argument may be, the broad codified language cannot be qualified better than by those who wrote the statute themselves. The legislature clearly and unequivocally intended the statute to allow “the court to award costs and attorney’s fees to a trustee who *prevails* in an action.”<sup>183</sup> Even though the codified language of section 114.064 provides a broader scope than the legislative intent, the codified language does not divorce itself from the legislature’s qualifying intent to award attorney’s fees and costs to a *prevailing* trustee.<sup>184</sup> It is also quite possible that the legislature assumed that this broader language would not result in courts finding the equitable-and-just requirement applicable to a non-prevailing trustee in a removal or surcharge action.

Lastly, it may be that the differing codified language was an attempt to follow language used in the Texas Civil Practice and Remedies Code, which states, “[i]n any proceeding under this chapter, the court may award costs and reasonable and necessary attorney’s fees as are equitable and just.”<sup>185</sup> The analogous language in the Trust Code and the Civil Practice and Remedies Code was codified at the same time in 1985.<sup>186</sup> Therefore, the Texas Legislature may have departed from its stated intent because of a desire to have similar language in both codes. In fact, Texas courts have utilized these statutes congruently.<sup>187</sup>

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(asserting that a matter must be properly brought under the Trust Code in order for section 114.064 to apply).

181. *Williams v. Northrup*, 649 S.W.2d 740, 747 (Tex. App.—Tyler 1983, writ ref’d n.r.e.).

182. *See* SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985) (noting that executors and administrators may recover attorney’s fees “in an action for removal or surcharge,” but prevailing trustees may not).

183. *Id.* (emphasis added).

184. *See* PROP. § 114.064 (reiterating the broader codified language rather than the legislative intent).

185. TEX. CIV. PRAC. & REM. CODE § 37.009 (West 2008).

186. *Id.*; PROP. § 114.064.

187. *See, e.g., In re Lesikar*, 285 S.W.3d 577, 584 (Tex. App.—Houston [14th Dist.]

Nevertheless, the clear intent of Trust Code section 114.064, which was to allow “the court to award costs and attorney’s fees to a trustee who prevails in an action for removal or . . . surcharge,” should not be disregarded merely because the Texas Legislature may have desired similar language in both codes.<sup>188</sup>

The question looms as to why the legislature codified language different than its stated intent.<sup>189</sup> Although the legislature refers to the Probate Code as a reason why the statute may be necessary, the disarray of case law interpreting vague and varying statutes as well as the distinct differences between Trust Code section 114.064 and other Probate Code provisions, illustrates that the codified language was not an attempt to create a statute parallel to the Probate Code.<sup>190</sup> Further, a strong argument could be that the varying language was due to the legislature’s attempt to create a broad grant of attorney’s fees in trust litigation. Finally, the legislature may have desired to have analogous language in the Trust Code and Civil Practice and Remedies Code; however, the unequivocal intent of the legislature was to grant attorney’s fees to a prevailing trustee.<sup>191</sup>

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2009, no pet.) (utilizing the Texas Civil Practice and Remedies Code congruently with the Texas Trust Code); *In re Ray Ellison Grandchildren Trust*, 261 S.W.3d 111, 127 (Tex. App.—San Antonio 2008, pet. denied) (utilizing both the Civil Practice and Remedies Code and the Trust Code in a trust and will controversy); *Lesikar v. Moon*, 237 S.W.3d 361, 375 (Tex. App.—Houston [14th Dist.] 2007, pet. denied) (analyzing the award of attorney’s fees under both the Civil Practice and Remedies Code and Trust Code); *Lyc0 Acquisition 1984 Ltd. v. First Nat’l Bank of Amarillo*, 860 S.W.2d 117, 119–22 (Tex. App.—Amarillo 1993, writ denied) (reducing the issue of attorney’s fees to a determination made using both the Civil Practice and Remedies Code and Trust Code).

188. SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985).

189. *See id.* (explaining that the purpose of Trust Code section 114.064 was to allow “the court to award costs and attorney’s fees to a trustee who prevails in an action for removal or surcharge”). *But see* PROP. § 114.064 (differing from the stated intent by mandating that “[i]n any proceeding under this code the court may make such award of costs and reasonable and necessary attorney’s fees as may seem equitable and just”).

190. *Compare* *Fillion v. Osborne*, 585 S.W.2d 842, 845 (Tex. Civ. App.—Houston [1st Dist.] 1979, no writ) (interpreting Probate Code section 245 “to insure that the estate will not be charged with fees or any costs which are incurred by reason of fault of the personal representative”), *with* *Klein v. Klein*, 641 S.W.2d 387, 390 (Tex. App.—Dallas 1982, no writ) (implying that if the executor acts in good faith in defense of a suit, then the Probate Code provides for an award of attorney’s fees from the estate). The contradictory results of these cases, in analyzing statutory language from the Probate Code, illustrate why the legislature would not want to create a similar statute in the Trust Code.

191. *See* SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985) (describing the purpose of Trust Code section 114.064 was to allow

### C. *The Interplay Fails to Provide a Clear Rule*

Lastly, the current interplay matters because it results in an unclear rule from the varying use of common law and statutory rules.<sup>192</sup> This interplay causes needless litigation, and “[i]t is common knowledge that Americans have become extremely litigious and that our court system is floundering in a sea of civil cases.”<sup>193</sup> Additionally, “[w]hat is less well known is that the court activity includes not only tort claims such as personal injury, but also lawsuits involving wills and trusts.”<sup>194</sup> The result is that practitioners in trust and estate litigation have seen a steady increase in suits concerning trust and estate matters.<sup>195</sup> Reports are common from trust and estate firms of staggering increases in the amount of litigation they handle.<sup>196</sup> Indeed, one attorney reported, “a direct correlation between the bad economy over the

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“the court to award costs and attorney’s fees to a trustee who *prevails* in an action for removal or surcharge” (emphasis added)).

192. See *Hachar v. Hachar*, 153 S.W.3d 138, 142–44 (Tex. App.—San Antonio 2004, no pet.) (evaluating whether to grant attorney’s fees using Trust Code section 114.064). *But see* *Stone v. King*, No. 13-98-022-CV, 2000 WL 35729200, at \*8 (Tex. App.—Corpus Christi Nov. 30, 2000, pet. denied) (not designated for publication) (utilizing the common law reasonableness test after codification of the statutory test). This illustration of the court’s varying use of rules to determine the same issue demonstrates how difficult it is for attorneys and litigants to judge the success or failure of their case when they do not even know what law will apply.

193. Bob Sacks, *Family Feuds*, PRIVATE WEALTH, Dec. 2008/Jan. 2009, available at <http://www.fa-mag.com/component/content/article/4694.html?issue=126&magazineID=3&Itemid=226>. Needless litigation can be best illustrated by *American National Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 212–13 (Tex. Civ. App.—Beaumont 1954, writ ref’d n.r.e.). There, the court explained that the principal matter was decided in *Mitchell*, where the court remanded the case to the trial court which entered a decree that was then appealed). See *id.* After the court determined the underlying case, subsequent litigation caused thousands of dollars in attorney’s fees, which could have been avoided if a clear rule as to attorney’s fees had been in place.

194. Bob Sacks, *Family Feuds*, PRIVATE WEALTH, Dec. 2008/Jan. 2009. See generally John E. O’Grady, *Guide to Preventing Inheritance Feuds with a No-Contest Clause*, O’GRADY LAW GROUP, APC (2010), [http://www.ogradylaw.com/articles/discourage\\_an\\_inheritance\\_fight\\_with\\_a\\_no\\_contest\\_clause.html](http://www.ogradylaw.com/articles/discourage_an_inheritance_fight_with_a_no_contest_clause.html) (providing that over the last twenty years, litigation regarding trusts and estates has been steadily increasing).

195. Bob Sacks, *Family Feuds*, PRIVATE WEALTH, Dec. 2008/Jan. 2009 (“Practitioners in the field of estate and trust litigation have seen a dramatic increase in recent years in lawsuits concerning probate estates and trusts . . .”).

196. Kelly Greene, et al., *Trust-Fund Kids Get Assertive in Down Market*, WALL ST. J., Dec. 17, 2002, at D1.

last three years and an increase in estate contests and trust contests.”<sup>197</sup>

To illustrate the dramatic figures in Texas, the Bexar County probate courts had 4,291 cases and 3,703 hearings filed in 2010.<sup>198</sup> Considering that the Bexar County probate courts only have a staff of twelve, there were 358 cases and 309 hearings per staff member.<sup>199</sup> Similarly, Travis County had over 313 cases and hearings per staff member.<sup>200</sup> Dallas and Harris Counties both had over 200 cases and hearings per staff member.<sup>201</sup> The overwhelming caseloads plaguing Texas probate courts will likely continue to rise, especially when considering the increasing population. For example, in 2010 the Bexar County population was 1,037,948—a 65.2% increase from 1983.<sup>202</sup>

In recent years, the Supreme Court of the United States has made a conscious effort to provide clear statements of the rules that it sets forth. Texas courts should follow this trend to impede the incoming freight train that is the excessive backlog of litigation.<sup>203</sup> Not only do clear rules result in more consistent court decisions, but they also allow attorneys to better judge the success and failure of cases, in turn reducing court time, waste, and costs.<sup>204</sup> The interest of justice in Texas is better served by providing a clear rule for courts to use in determining attorney’s fees in trust litigation.

197. *Id.*

198. Memorandum from Dan Crutchfield, Investigator for Bexar County Probate Court #2, Probate Courts Staffing—Largest Counties of Texas (July 2011) (on file with the *St. Mary's Law Journal*).

199. *Id.*

200. *Id.*

201. *Id.*

202. *Id.*

203. *Cf.* John F. Manning, *Clear Statement Rules and the Constitution*, 110 COLUM. L. REV. 399, 399 (2010) (“In recent years, the Supreme Court has increasingly supplemented traditional Marbury-style judicial review with constitutionally inspired clear[-]statement rules.”).

204. *See* *Paulson v. State*, 28 S.W.3d 570, 571 (Tex. Crim. App. 2000) (establishing that judicial consistency contributes to the successful judicial process). Specifically, *Paulson* cautions that, “[w]e should not frivolously overrule established precedent. We follow the doctrine of *stare decisis* to promote judicial efficiency and consistency, encourage reliance on judicial decisions, and contribute to the integrity of the judicial process.” *Id.* (citing *Proctor v. State*, 967 S.W.2d 840, 845 (Tex. Crim. App. 1998)). However, the court clarifies that “if we conclude that one of our previous decisions was poorly reasoned or is unworkable, we do not achieve these goals by continuing to follow it.” *Id.*

## V. THE FORWARD-INCENTIVE RULE AND ITS INCORPORATION

### A. *The Forward-Incentive Rule and Implementation*

The broad brush with which Trust Code section 114.064 paints is that of awarding attorney's fees in a broad range of cases, not just the narrow scope focused on in this Comment.<sup>205</sup> Thus, the importance of the section must be respected and not rendered void because of some disparate results.<sup>206</sup> The remedy to the current interplay must take into consideration that the interplay is not simply between Trust Code sections 114.063 and 114.064, but also case law's test focused on the reasonableness and good faith of the trustee.<sup>207</sup> Therefore, the remedy to the current interplay must provide an avenue to preserve the benefits of sections 114.063 and 114.064 while also reconciling accompanying case law.

The remedy to the current interplay is the addition of the following language to Trust Code section 114.064:

In an action properly brought under the Texas Trust Code against a trustee by an interested party, if the trustee is found to have breached a fiduciary duty owed a trust beneficiary, or is found to have committed a breach of trust, or is removed with cause, the granting of attorney's fees from trust funds or individually from trust beneficiaries shall not be allowed.<sup>208</sup>

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205. See *In re Watson*, 325 B.R. 380, 388 (Bankr. S.D. Tex. 2005) (applying section 114.064 to trustees in bankruptcy actions).

206. See Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (establishing the disparate result of *Hachar v. Hachar* that is the consequence of section 114.064, which provides a means for a trustee to recover attorney's fees from trust funds, even though a court deems the trustee breached a fiduciary duty).

207. See *Grey v. First Nat'l Bank*, 393 F.2d 371, 387 (5th Cir. 1968) (continuing to follow *American National Bank of Beaumont v. Biggs* when stating that "a trustee may charge his trust for attorney's fees which the trustee, acting reasonably and in good faith, incurs in defense of litigation charging him with a breach of trust").

208. Compare *In re Watson*, 325 B.R. at 388 ("A trustee commits a breach of trust if he fails to carry out the express terms of a trust."), and *Ertel v. O'Brien*, 852 S.W.2d 17, 21 (Tex. App.—Waco 1993, writ denied) ("A trustee commits breach of trust not only where he violates a duty in bad faith, or intentionally although in good faith, or negligently[,] but also where he violates a duty because of a mistake."), *aff'd sub nom. Citizens Bank & Trust Co. of Baytown v. Ertel*, No. 01-98-00548-CV, 2001 WL 26141 (Tex. App.—Houston [1st Dist.] Jan. 11, 2001, pet. denied) (not designated for publication), with TEX. PROP. CODE ANN. § 113.082 (West 2007) (expressing that a trustee may be removed on the petition of an interested party "if the trustee materially violated or attempted to violate the terms of the trust and the violation or attempted violation results in a material financial loss to the trust," or "the trustee fails to make an accounting that is required by law or by the terms of the trust," or "the court finds other cause for removal"), and Huie

This qualifying language—referred to as the forward-incentive rule—retains the necessary language for attorneys to be awarded fees for other matters within the Trust Code, but strips the power of the courts to entertain awarding attorney's fees to a trustee who is removed with cause or is found to have breached a duty owed.<sup>209</sup> Codification of this language would also obligate courts to follow the rule in lieu of previous case law.<sup>210</sup> Establishment of the forward-incentive rule simply qualifies the current statutory language while obligating Texas courts to follow the rule.

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v. DeShazo, 922 S.W.2d 920, 921 (Tex. 1996) (asserting that trustees owe fiduciary duties to trust beneficiaries and failure to comply with these duties renders the trustee liable for damages). These laws illustrate the three cornerstones of trustee misconduct: breaching trust, breaching a fiduciary duty, and removal with cause. The intent of incorporating these cornerstones into the forward-incentive rule is to encompass all facets of trustee misconduct and to prevent the awarding of attorney's fees to neglectful trustees.

209. See PROP. § 114.064 (West 2007) (showing the current language regarding attorney's fees in trust litigation). Under the forward-incentive rule, this statute would be qualified by disallowing the court to award attorney's fees from the trust to a trustee who is either removed with cause or is shown to have breached a duty owed to the beneficiary.

210. See AMY E. SLOAN, BASIC LEGAL RESEARCH: TOOLS AND STRATEGIES 4 (Vicki Been et al. eds., 4th ed. 2009) (writing that courts are "obligated to apply the rule from the statute, not the former common law rule"). The forward-incentive rule would place upon courts the obligation to follow the statute and not follow rules from past cases such as *Biggs* and *Hachar*. See, e.g., *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 220–21 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (adopting the test that if the trustee acts reasonably and in good faith, an award of attorney's fees out of trust corpus is appropriate); Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (reiterating that *Hachar* reminds litigants that neglectful trustees can be awarded attorney's fees from the trust, even if they are removed with cause or are deemed to have breached a duty owed to the beneficiary). However, an argument could be made that Texas courts have not followed section 114.064 in all cases coming under the Trust Code since its codification. This begs the question of whether courts will ignore the forward-incentive rule as well. See *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*5 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication) (holding that "[u]nder Texas law, a trustee may charge the trust for attorney's fees the trustee, acting reasonably and in good faith, incurs defending charges of breach of trust," despite discussing section 114.064 at length). However, the distinguishing factor is that past courts have engaged in the interplay of case law and statutes because they view the two rules as one-and-the-same. See *id.* at \*4 (showing that the only logical resolution to the court's use of the common law rule, instead of the statutory rule, was that the court found both rules to be identical). The forward-incentive rule would be followed unequivocally because the forward-incentive rule is not similar to other laws and is a qualifier from current statutory and common law.

### B. *The Forward-Incentive Rule Shifts the Necessary Incentives*

The current interplay provides little incentive for a beneficiary to bring suit against a trustee for compliance with the trustee's fiduciary duties.<sup>211</sup> One of the most basic purposes of laws is to incentivize citizens to act in accordance with promulgated rules.<sup>212</sup> For example, the Texas Trust Code provides that "a trustee who commits breach of trust is chargeable with any damages resulting from such breach of trust."<sup>213</sup> This law incentivizes trustees to not breach their fiduciary duties or they must pay damages to the beneficiary.<sup>214</sup> The forward-incentive rule addresses and places the incentives with the appropriate parties so that the trustee has an incentive to act in accordance with fiduciary duties, and beneficiaries have an incentive to sue when the trustee breaches these duties.

The forward-incentive rule provides an unequivocal incentive for trustees to not breach their duties. Not only will there be damages owed, but trustees will also not be entitled to have their attorney's fees reimbursed.<sup>215</sup> Additionally, the forward-incentive rule gives a vital incentive to trust beneficiaries. The incentive is two-fold: first, it encourages beneficiaries to sue when they

211. See Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (concluding that the end result of *Hachar* "reminds litigants that any party involved in trust litigation should seek an award of attorney's fees under Trust Code section 114.064 because the court has the authority to award fees even in favor of the losing party if the court believes that it is equitable and just"). This discourages beneficiaries from bringing suit against a trustee knowing that even if they win the suit, the trustee likely is going to be awarded attorney's fees out of the trust. *Id.* From a purely economic standpoint, rarely will the benefits of recovery outweigh the costs in pursuit of recovery.

212. See *Robinson v. Brice*, 894 S.W.2d 525, 528 (Tex. App.—Austin 1995, writ denied) (acknowledging the importance of incentives in law by stating that "the prejudgment-interest statute provides a series of incentives designed to encourage the expeditious settlement of claims").

213. PROP. § 114.001(c) (West 2007).

214. *Id.*

215. See Melanie B. Leslie, *Common Law, Common Sense: Fiduciary Standards and Trustee Identity*, 27 CARDOZO L. REV. 2713, 2717 (2006) (noting that monitoring a trustee can be very expensive, and "the trustee is largely immune from outside pressures"). The costly nature of oversight is not the only problem. In order to "evaluate whether the trustee is exercising the requisite level of care, the beneficiary would need to possess the same level of expertise and skill as the trustee itself." *Id.* at 2718. The inherently complicated and costly nature of oversight does not provide adequate protection to the beneficiary, but the forward-incentive rule changes this by acting as a shield of protection. The trustee will know that a breach of duty will result in damages without the possibility of reimbursement for attorney's fees.

reasonably believe the trustee has breached a duty; and second, it discourages beneficiaries from suing when there is a low likelihood of prevailing in a suit. For example, consider a beneficiary who suspects his trustee is engaging in multiple self-dealing transactions that are a breach of the trustee's duties.<sup>216</sup> The forward-incentive rule incentivizes the beneficiary to bring suit only for those transactions that likely can be proven were improper, while forgoing suit for those transactions that likely cannot be proven. The forward-incentive rule provides these incentives because if the beneficiary pleads causes of actions with merit, the likelihood of the trustee being found not to have breached a duty is minimal; thus, the likelihood of paying the trustee's attorney's fees from the trust is minimal.<sup>217</sup> However, the incentive is also present in the converse: if the beneficiary brings a meritless suit, the likelihood of paying the trustee's attorney's fees out of trust funds is very high; thus, the beneficiary has an incentive to not bring claims with a low likelihood of success.<sup>218</sup>

### C. *The Forward-Incentive Rule Provides Clarity*

The addition of the forward-incentive rule's qualifying language to Trust Code section 114.064 remedies the current interplay by providing a clear rule for Texas courts. To illustrate the benefits of clear rules, consider how past cases would have fared if the language of the forward-incentive rule were codified in the 1985 version of section 114.064. Quite simply, because of the clear

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216. See *Chien v. Chen*, 759 S.W.2d 484, 495 (Tex. App.—Austin 1988, no writ) (acknowledging that common law recognizes a “general prohibition against the fiduciary’s using the relationship to benefit his personal interest, except with the full knowledge and consent of the principal”).

217. See *id.* (rejecting the petitioner’s appeal and criticizing his frivolous abuse of the system). The court describes the petitioner’s argument as “a hodgepodge of unsupported assertions, irrelevant platitudes, and legalistic gibberish.” *Id.* Although the court admonished such frivolous claims, it also reaffirmed the importance of “the courts to remain open to all who seek in good faith to invoke the protection of law.” *Id.*

218. For case examples of the consequences of frivolous suits brought by beneficiaries, see ALAN NEWMAN, ET AL., *THE LAW OF TRUSTS AND TRUSTEES* § 971, at 366 (3d ed. 2010). This section of the treatise offers a discussion of what is “[u]sually required for the trustee’s legal fees to be charged against the beneficial interests of unsuccessful objecting beneficiaries . . . .” *Id.* Although the authors exemplify instances where beneficiaries were charged after bringing an unsuccessful suit, the Texas Supreme Court has explicitly provided that Trust Code section 114.064 does not require the party awarded fees to have prevailed in the underlying suit. *Hachar v. Hachar* 153 S.W.3d 138, 142 (Tex. App.—San Antonio 2004, no pet.).



language in the forward-incentive rule, cases such as *Hachar*, *Moody*, and *Stone*, would not have needed judicial intervention to determine whether the granting of attorney's fees to the trustee was proper.<sup>219</sup> The matter would resolve itself if at the trial level the trustee was deemed to have breached a duty owed the beneficiary or was removed with cause. Similarly, the forward-incentive rule provides clear language that no further judicial process is necessary to determine attorney's fees for the wrongdoing trustee. Application of the forward-incentive rule to cases prior to codification of section 114.064 is even more illustrative. For example, the issue in *Biggs* was whether the award of attorney's fees to the trustees was proper after it was deemed that the trustees acted improperly in administering a trust.<sup>220</sup> Under the forward-incentive rule the entire case of *Biggs* would likely have been avoided because the disposition of the underlying case—that the trust was improperly administered—negates any opportunity for the trustee to be awarded attorney's fees.<sup>221</sup>

The forward-incentive rule also provides clarity by providing a single source for judges when determining the award of attorney's fees in trust litigation. The current interplay is detrimental because Texas courts presently use a hodgepodge of rules to determine whether to grant attorney's fees to trustees.<sup>222</sup> Thus,

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219. See *Hachar*, 153 S.W.3d at 142 (exploring whether attorney's fees could be awarded to a trustee who had been removed for misadministration of the trust); *Stone v. King*, No. 13-98-022-CV, 2000 WL 35729200, at \*8, \*13-14 (Tex. App.—Corpus Christi Nov. 30, 2000, pet. denied) (not designated for publication) (considering whether the granting of attorney's fees to a trustee who breached his fiduciary duty was proper); *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*1 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication) (evaluating whether attorney's fees could be awarded to a trustee who engaged in self-dealing).

220. See *Am. Nat'l Bank of Beaumont v. Biggs*, 274 S.W.2d 209, 212-13 (Tex. Civ. App.—Beaumont 1954, writ ref'd n.r.e.) (proclaiming the case arose “from a decree which authorizes the trustees of the Aurelia Mitchell Trust to pay a fee to certain lawyers for legal services rendered by these lawyers in [the underlying suit]”). If the qualifying language of the forward-incentive rule were applicable at the time the underlying suit was decided, *Biggs* would not have been filed because the breaching trustee would be statutorily precluded from an award of attorney's fees. See *id.* at 221 (awarding attorney's fees to trustees despite a mismanagement of the trust).

221. See *id.* at 219 (recounting material matters from a prior case involving former trustees and finding the award of attorney's fees proper despite the trustees' erroneous administration of the trust).

222. See *Stone*, 2000 WL 35729200, at \*8 (utilizing prior precedent after codification of Trust Code section 114.064 to determine the issue that the statute was created to address); see also *Moody*, 1999 WL 1041541, at \*5-9 (claiming to apply section 114.064,

reliance on judicial decisions is tenuous for parties in trust litigation. Further, the decision of whether to take a matter to trial is blurred because the parties are unsure of what rules the court will apply.<sup>223</sup> Consequently, the forward-incentive rule will cut down on litigation and court resources by advancing a statute that encourages consistent judicial application and reliance on the rule by trust parties.

#### D. *The Forward-Incentive Rule Provides Equity*

Texas courts, in large part, fail to comprehend that when a beneficiary is successful in a suit against a trustee, yet attorney's fees are awarded to the trustee from the trust, the beneficiary loses despite winning the underlying suit.<sup>224</sup> One Texas court dismissively referred to this as a "supposed injustice."<sup>225</sup> The inherent injustice suffered by the harmed beneficiary—both economically and judicially—could be avoided with the implementation of the forward-incentive rule.

The language of the forward-incentive rule negates the possibility that a trustee who has breached a duty or who is removed with cause will be awarded attorney's fees from trust funds in defense of neglectful conduct. Additionally, it prevents an attempt to recover attorney's fees from a trust beneficiary personally. Further, the forward-incentive rule does not penalize the beneficiary, who is considered the "real owner," of the trust property when the beneficiary successfully proves its case.<sup>226</sup> As stated above, clearly established Texas law grants that trust beneficiaries possess "true equitable title as against the trustee, who is a mere holder of the naked legal title at the convenience of the beneficiary."<sup>227</sup> Therefore, the forward-incentive rule

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but actually applying the common law test).

223. *See Paulson v. State*, 28 S.W.3d 570, 571 (Tex. Crim. App. 2000) (promoting judicial consistency as a contribution to the successful judicial process).

224. *See Shearrer v. Holley*, 952 S.W.2d 74, 78 (Tex. App.—San Antonio 1997, no writ) (stating that because legal and beneficial title are separated, if the assets of the trust dwindle, the person who benefits from the trust—the beneficiary—is the harmed party).

225. *See Biggs*, 274 S.W.2d at 219 (addressing a beneficiary's assertion that the wrongful act of a trustee should not be charged to all beneficiaries to the trust).

226. *See Faulkner v. Bost*, 137 S.W.3d 254, 258 (Tex. App.—Tyler 2004, no pet.) (referring to the beneficiary as the "real owner" while deeming the trustee as holder of "bare legal title").

227. *Hall v. Rawls*, 188 S.W.2d 807, 815 (Tex. Civ. App.—Beaumont 1945, writ ref'd w.o.m.).

alleviates judicial injustice by disallowing a trustee to be paid attorney's fees from trust funds when the trustee is found to have breached a fiduciary duty. Similarly, the forward-incentive rule remedies the economic injustice of the current interplay. Trust Code section 114.001 illustrates one of the overriding principles of trust law, to make a wronged beneficiary whole.<sup>228</sup> The current interplay does not make the injured beneficiary whole; however, the forward-incentive rule does.<sup>229</sup> Therefore, the forward-incentive rule is congruent with existing trust principles and Texas law, which assert that a wronged beneficiary should be made whole for the negligence of the trustee, while further capturing the concepts of equity.<sup>230</sup>

#### E. *The Forward-Incentive Rule Follows the Intent of the Texas Legislature*

Trust Code section 114.064 was codified because “the current [c]ode does not contain a provision allowing the court to award costs and attorney's fees to a trustee who prevails in an action for removal or . . . surcharge.”<sup>231</sup> This unambiguous assertion found

228. See TEX. PROP. CODE ANN. § 114.001(c) (West 2007) (stressing that “[a] trustee who commits a breach of trust is chargeable with any damages resulting from such breach of trust[.]” which in turn makes whole a wronged beneficiary).

229. See *id.* (stating that if a trustee commits a breach of trust, he may be liable for the damages that result, which in turn, makes whole a wronged beneficiary). The existing statutory interplay's inability to provide the beneficiary with an adequate remedy, compared to the forward-incentive rule's potential to make the beneficiary whole is best illustrated by example. Consider a trust that has assets of \$1,000,000. Through the trustee's negligence, the value drops 25% to \$750,000. Attorney's fees for defending the trustee's actions that caused the reduction are estimated to cost approximately \$200,000. The beneficiary proves a breach of fiduciary duty claim. Following the interplay, the court allows the trustee's attorney's fees to be awarded out of the trust; thus, the net result after litigation would be the trust corpus valued at \$550,000, a 45% loss. Following the forward-incentive rule, attorney's fees could not be awarded; thus, the trust value would remain at \$750,000, a 25% loss. However, in both situations the trustee returns the \$250,000 as a result of the breach. See *id.* (charging a trustee for damages resulting from a proven breach of trust). For the court using the interplay, this would bring trust corpus back to \$800,000 resulting in total loss of \$200,000, or 20%, for the *winning* beneficiary. However, the use of the forward-incentive rule would result in the reimbursement of the \$250,000 to the trust, and the beneficiary being made completely whole.

230. See *id.* (charging a trustee with damages resulting from a breach of trust); *Texarkana Nat'l Bank v. Brown*, 920 F. Supp. 706, 713 (E.D. Tex. 1996) (granting attorney's fees to beneficiaries after a successful action against the trustee bank for negligent administration and breach of trust).

231. SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985).

in the senate committee's bill analysis expresses the intent of the Texas Legislature to codify a law that provides attorney's fees to a prevailing trustee, not a desire to create a law to award attorney's fees to a non-prevailing trustee.<sup>232</sup> However, because the Texas Legislature failed to codify language that encompassed its stated intent, the qualifying language of the forward-incentive rule is necessary to apply this in practice. This language ensures courts do not step outside the bounds of the statute's intent and award attorney's fees to non-prevailing trustees in a removal or surcharge action.<sup>233</sup>

## VI. CONCLUSION

The current interplay between Texas Trust Code sections 114.063 and 114.064 and accompanying case law has resulted in convoluted and inconsistent tests for determining whether a trustee is entitled to attorney's fees for defending a suit that successfully proves the trustee breached a fiduciary duty.<sup>234</sup> As a result, trust beneficiaries often are faced with a lose-lose situation when enforcing their rights against trustee misconduct.<sup>235</sup>

However, the current interplay and the resulting inequities can be corrected by implementing the qualifying language of the

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232. *See id.* (purporting that the reason for codification of section 114.064 was to award attorney's fees to a trustee prevailing in a removal or surcharge action). The stated intent does not provide for the award of attorney's fees to a trustee who does not prevail in a removal or surcharge action. *Id.*

233. By specifying that attorney's fees are not to be awarded to a trustee in a case where the trustee breached a duty or was removed with cause, the forward-incentive rule harmonizes the existing statutory language with the express intent of the legislature. *Id.*

234. *See Hachar v. Hachar*, 153 S.W.3d 138, 140 (Tex. App.—San Antonio 2004, no pet.) (affirming attorney's fees to both the beneficiaries and the trustee in a suit brought by beneficiaries against the trustee for mismanagement); *Biggs*, 274 S.W.2d at 219 (awarding attorney's fees to the trustee who acted wrongfully, but not intentionally in mismanaging trust); *Moody Found. v. Estate of Moody*, No. 03-99-00034-CV, 1999 WL 1041541, at \*2-5 (Tex. App.—Austin Nov. 18, 1999, pet. denied) (not designated for publication) (illustrating the convoluted nature of the interplay by discussing that section 114.064 applies, but instead of applying the statutory test, applying the case law test to determine whether the granting of attorney's fees from trust funds was proper); Gerry W. Beyer, *Wills and Trusts*, 59 SMU L. REV. 1603, 1643 (2006) (presenting *Hachar* as a reminder that there is no requirement under section 114.064 that attorney's fees may only be granted to prevailing parties).

235. *Biggs*, 274 S.W.2d at 219 (“It is unjust . . . that [the beneficiary] won the suit and established royalties as corpus, but . . . must pay the fees out of [the] corpus for those who would have dissipated it.”).

forward-incentive rule into section 114.064. The forward-incentive rule provides a clear and equitable rule that shifts the necessary incentives to the correct parties by encouraging trustees to act in accordance with fiduciary obligations, while also emboldening beneficiaries to enforce their legal rights when the trustee acts wrongfully. The Texas Legislature expressed its intent regarding the awarding of attorney's fees in trust litigation through section 114.064; the legislature explained its intent to construct a provision to allow courts to award attorney's fees "to a trustee who prevails in an action for removal or surcharge."<sup>236</sup> The forward-incentive rule's qualifying language to section 114.064 conforms the existing statutory language to the legislature's original intent. Through implementation of the forward-incentive rule, judicial decisions will be more consistent, which will enable parties to better anticipate the outcome of a potential suit. The forward-incentive rule will decrease litigation and provide a remedy that makes wronged beneficiaries whole, thus enhancing the existing canons of trust law.

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236. SENATE COMM. ON STATE AFFAIRS, BILL ANALYSIS, TEX. S.B. 517, 69th Leg., R.S., at 1 (1985).