WILLS, TRUSTS, AND ESTATES

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I. INTRODUCTION

The 2011 session of the Virginia General Assembly enacted wills, trusts, and estates legislation that: (i) eliminated a potential federal transfer tax trap in *inter vivos* marital trusts, (ii) interpreted transfer tax formula clauses in light of recent changes in federal law, and (iii) adopted the Uniform Adult Guardianship and Protective Proceedings Jurisdiction Act. Three other legislative enactments and seven opinions of the Supreme Court of Virginia during the twelve months ending June 1, 2011, addressed issues affecting this field. In addition to addressing those developments, this article summarizes a recent federal district court opinion that dealt with a significant issue in Virginia trust administration.

II. LEGISLATION

A. *Creditor Protection for Certain Trusts*

1. Settlor's Retained Interest in *Inter Vivos* Marital Trust

When a settlor creates and funds an irrevocable trust for his or her spouse during his or her lifetime, the trust instrument often provides that the trust will continue for the settlor's benefit if he or she outlives the spouse. If the trust qualifies for the federal gift

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tax marital deduction,[1] a special federal tax rule treats the spouse as the creator of the trust for subsequent transfer tax purposes.[2] The value of the trust assets is thus subject to estate tax at the spouse's death. However, the rule is intended to protect the trust from estate tax at the settlor's death even if he or she is eligible to receive trust distributions because the spouse has died before the settlor.[3]

Virginia law, however, continued to treat the settlor as the creator of the trust.[4] The settlor's creditors therefore maintained their statutory right to reach any part of the marital trust that the trustee could distribute to the settlor after the spouse's death.[5] Any property that can be used to pay a decedent's debts is includable in the decedent's gross estate for federal estate tax purposes.[6] As a result, the existence of state creditor rights could cause a marital trust to be taxed again in the estate of a Virginia settlor who survives his or her spouse, contrary to the intent of the federal transfer tax rules. This rule reflects the law's traditional antipathy towards self-settled spendthrift trusts.

The 2011 session of the General Assembly corrected this problem by amending the Uniform Trust Code to include a specific exception allowing spendthrift protection for the settlor's interest in an *inter vivos* marital trust after the spouse's death.[7] Consistent with the principles of federal transfer tax, the revised Virginia rule treats the spouse as the creator of a qualifying marital trust.[8] Note, however, that although *inter vivos* marital deduction trusts are typically created for tax reasons, it is at least theoretically possible now to create a self-settled spendthrift trust for creditor

1. *See generally* I.R.C. § 2523(e), (f) (2006) (regarding general power of appointment and qualified terminable interest property trusts respectively).

2. *See id.* §§ 2044(c), 2523(f)(5), 2652(a) (regarding estate, gift, and generation-skipping transfer taxes respectively).

3. Many advisors take advantage of this rule in situations where one spouse does not have sufficient assets of his or her own to use the full estate tax exemption by having the wealthier spouse transfer assets to a marital deduction trust during his or her lifetime. To encourage the settlor spouse to fund such a trust, the terms often provide for the trust assets to be held in a trust for the settlor spouse's benefit if he or she survives the donee spouse.

4. *See* VA. CODE ANN. § 55-541.03 (Repl. Vol. 2007).

5. *See id.* § 55-545.05(A)(2) (Repl. Vol. 2007 & Cum. Supp. 2011).

6. *See* I.R.C. § 2041(a)(2) (2006).

7. Act of Mar. 22, 2011, ch. 354, 2011 Va. Acts ___ (codified at VA. CODE ANN. § 55-545.05(B)(3) (Cum. Supp. 2011)).

8. VA. CODE ANN. § 55-545.05(B)(3) (Cum. Supp. 2011).

protection purposes by funding a marital trust shortly before the spouse's death.

2. Beneficiary's Withdrawal Rights

To qualify gifts to irrevocable trusts as present interests eligible for the federal gift tax annual exclusion,[9] most settlors give the trust beneficiaries a limited right to withdraw part of each gift. If not effectively exercised within the prescribed time period, these powers typically lapse. For federal transfer tax purposes, the beneficiary is treated as making a gift back to the trust (thus becoming a settlor of the trust) only to the extent the lapsed power exceeds the greater of $5000 or 5% of the aggregate value of the assets subject to the power.[10]

Similarly, under Virginia law, the lapse, release, or waiver of a beneficiary's withdrawal right causes that beneficiary to be treated as a settlor of the trust—giving the beneficiary's creditors the same rights to reach his or her interest in the trust as if it were self-settled—only to the extent the beneficiary could withdraw more than the greater of the "5 and 5" amount and the gift tax annual exclusion amount.[11] This created a potential trap for beneficiaries whose withdrawal powers were defined in terms of the greater of the "5 and 5" amount and *twice* the federal gift tax annual exclusion amount so as to allow the settlor to elect with his or her spouse to "split" the gift.

The 2011 amendment to Virginia Code section 55-545.05 eliminated this problem by increasing the withdrawable amount not subject to creditor claims to twice the gift tax annual exclusion for trusts created by married settlors.[12]

9. *See* I.R.C. § 2503(b)(1) (2006). The current annual exclusion levels allow anyone to give an unlimited number of donees up to $13,000 each without gift tax consequences. A donor's spouse can enable the donor to double that annual limit by agreeing to treat a gift as if the spouse had made half of it, i.e., to "split the gift" with the donor. *See id.* § 2513(a).

10. *See id*. § 2514(e). The article refers to this as the "5 and 5" amount.

11. VA. CODE ANN. § 55-545.05(B)(2) (Repl. Vol. 2007 & Cum. Supp. 2011).

12. *See* ch. 354, 2011 Va. Acts ___.

B. *Formula Clauses Based on Federal Transfer Tax Concepts*

Federal transfer tax legislation enacted in 2001 repealed the estate and generation-skipping transfer ("GST") taxes, beginning January 1, 2010, and modified the rules for determining the tax basis of inherited property for one year.[13] This action raised questions about the interpretation of tax formula clauses in the estate planning documents of decedents who died in 2010, when the statutory concepts to which the clauses referred were not part of federal tax law.[14] The 2010 General Assembly quickly and effectively addressed that issue by enacting a rule of construction that treated such clauses as referring to the federal rules in effect on December 31, 2009.[15]

The 2010 amendment provided in part:

> A will or trust of a decedent who dies after December 31, 2009, and before January 1, 2011, that contains a formula referring to. . . any section of the Internal Revenue Code relating to the federal estate tax or [GST] tax, or that measures a share of an estate or trust based on the amount that can pass free of federal estate taxes or the amount that can pass free of federal [GST] taxes . . . shall be deemed to refer to the federal estate tax and [GST] tax laws as they applied with respect to estates of decedents dying on December 31, 2009. . . . If the federal estate or generation-skipping transfer tax becomes effective before that date, the reference to January 1, 2011, in this subsection shall refer instead to the first date on which such tax becomes legally effective.[16]

In late 2010, Congress reinstated the federal estate and GST taxes retroactive to January 1, 2010, and raised the applicable exemption amounts to $5 million for decedents dying in 2010.[17] Personal representatives of those who died in 2010, however, could choose between the reinstated estate tax system and the pre-

13. *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, §§ 501, 541, 542, 115 Stat. 38, 69, 76–86 (2001) (codified as amended at I.R.C. §§ 1014(f), 1022, 2210 (2006)).

14. *See id.*

15. *See* Act of Apr. 7, 2010, ch. 238, 2010 Va. Acts 330 (codified at VA. CODE ANN. § 64.1-62.4 (Cum. Supp. 2010)); *see also* J. Rodney Johnson, *Annual Survey of Virginia Law: Wills, Trusts, and Estates,* 45 U. RICH. L. REV. 403, 408–09 (2010) (discussing the original 2010 legislation addressing the one-year repeal of the federal estate tax).

16. Ch. 238, 2010 Va. Acts at 330.

17. *See* Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, §§ 301–303, 124 Stat. 3296, 3300–04.

existing modified tax basis system.[18] These federal changes raised two questions: (i) whether tax formulas now should be interpreted through reference to the 2010 rules, and (ii) whether their interpretation should depend on which tax system the personal representative chose for the estate.

The 2010 Virginia statute would have interpreted many formula clauses as referring to the 2009 maximum exemption of $3.5 million, even though Congress had increased the exemption to $5 million for those dying in 2010.[19] In some instances, a larger exemption would have provided more protection against transfer tax liability, but in others it might have led to the disinheritance of spouses and other beneficiaries as a result of the substantial increase in estate and GST tax exemptions between 2008 ($2 million) and 2010 ($5 million).[20] The personal representative's ability to affect the interpretation of a tax formula—and thus the beneficiaries' shares—by choosing federal tax rules could also present significant fiduciary duty issues as the representative tried to determine which tax system would more fairly balance the interests of all beneficiaries.

The 2011 amendment to Virginia Code section 64.1-62.4 attempts to provide an immediately effective set of rules that avoids those fiduciary issues.[21] A formula clause in a will, trust, or other instrument referring to federal transfer tax concepts is deemed to refer to the transfer tax laws effective in 2010 whether or not the decedent's personal representative elects to have the estate tax apply, unless the instrument manifests an intent to apply a contrary rule.[22]

The amendment, however, also provides beneficiaries with a mechanism to establish that a particular decedent intended another result. Any fiduciary or affected beneficiary under the instrument may seek a judicial determination that the decedent in-

18. *See id.* at § 301.

19. *Compare id.* (referring to 2010 tax information), *with* I.R.C. § 2010 (2006) (referring to 2008 tax information).

20. *Compare* Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act § 302, *with* I.R.C. § 2010 (2006).

21. Act of Mar. 26, 2011, ch. 679, 2011 Va. Acts ___ (codified as amended at VA. CODE. ANN. § 64.1-62.4 (Cum. Supp. 2011)) (including an emergency clause making the amendment effective as of the date of passage).

22. *Id.*

tended the instrument to be construed in a different manner.[23] Any such proceeding must be brought before January 1, 2012, regardless of when in 2010 the decedent died.[24] The person bringing the proceeding has the burdens of proof and persuasion in establishing the decedent's intent and must prove by clear and convincing evidence that the decedent did not intend the statutory default rule to apply.[25]

Given Virginia's traditional adherence to the "four corners" doctrine,[26] it is perhaps surprising that the amendment expressly authorizes the court to "consider extrinsic evidence that contradicts the plain meaning of the . . . instrument."[27] It also authorizes the court to modify the instrument retroactively to the decedent's death, as needed to conform to the decedent's intention or to "achieve the decedent's tax objectives in a manner that is not contrary to the decedent's probable intention."[28] As an alternative, "interested persons may enter into a binding agreement"—which in the case of a trust may be in the form of a nonjudicial settlement agreement under Virginia Code section 55-541.11—that the decedent intended a contrary construction and may conform the terms of the instrument to that intention without court approval.[29]

Such judicial and nonjudicial interpretations of a decedent's intent should bind the parties and confirm their respective property rights. It remains to be seen, however, whether such a judicial modification or interpretation, and particularly a nonjudicial settlement agreement, may be subject to challenge by the Internal Revenue Service.[30]

23. *Id.*

24. *See id.*

25. *Id.*

26. *See, e.g.*, Wilson v. Holyfield, 227 Va. 184, 187–88 (1984).

27. Ch. 679, 2011 Va. Acts. ___.

28. *Id.*

29. VA. CODE ANN. § 64.1-62.4(C) (Cum. Supp. 2011) (noting that such agreements also may be approved by the court if the beneficiaries wish).

30. *See* Comm'r v. Estate of Bosch, 387 U.S. 456, 457 (1967) (holding that federal tax authorities are not bound by a determination of property rights made by a state trial court).

C. *Adult Guardianships and Protective Proceedings*

Following the lead of twenty-two other states and the District of Columbia, the 2011 General Assembly enacted the Uniform Adult Guardianship and Protective Proceedings Jurisdiction Act.[31] The legislation establishes rules for resolving multistate jurisdictional disputes, facilitating transfers of a guardianship or conservatorship arrangement to another state or country, and enforcing related court orders across jurisdictional lines. The Act encourages communication and cooperation between Virginia courts and those of other states and foreign countries, and establishes rules for determining which court has jurisdiction in particular instances.[32] The Act seeks to avoid conflicts and "forum shopping" by ensuring that only one state has jurisdiction at any given time.[33]

1. Jurisdictional Rules

A Virginia court may appoint a guardian or issue a protective order appointing a conservator for an adult who has been physically present in the commonwealth, including periods of temporary absence, for the six-month period immediately preceding the petition.[34] A Virginia court also may exercise jurisdiction over any adult with other significant connections to Virginia, including family or property in the commonwealth, or other ties such as voter registration, vehicle registration, driver's license, tax return filing, social relationships, or receipt of services, but only if the adult does not have a home state (or a court of that state has declined to exercise jurisdiction because Virginia is a more appropriate forum) or no petition is pending in the adult's home state and no objection is filed by a person required to be notified.[35]

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31. Act of Mar. 25, 2011, ch. 518, 2011 Va. Acts ___ (codified at VA. CODE ANN. §§ 37.2-1031 to -1052 (Repl. Vol. 2011)). To date, twenty-nine states and the District of Columbia have enacted the uniform law, with another five having introduced legislation for consideration in 2011. *Legislative Fact Sheet—Adult Guardianship and Protective Proceedings Jurisdiction Act*, UNIFORM LAW COMMISSION, http://www.nccusl.org/LegislativeFactSheet.aspx?title=AdultGuardianshipandProtectiveProceedingsJurisdictionAct (last visited Oct. 12, 2011).

32. *See* ch. 518, 2011 Va. Acts ___.

33. *See id.*

34. VA. CODE ANN. §§ 37.2-1037(a), -1039 (Repl. Vol. 2011).

35. *Id.* §§ 37.2-1037(b), -1039(2) (Repl. Vol. 2011).

Virginia courts also may act if: (i) courts in the adult's home state and all significant connection states have determined that Virginia is the more appropriate forum,[36] or (ii) an emergency requires appointment of a temporary guardian for an adult physically present in the commonwealth, a protective order is needed for property located here, or a guardianship or conservatorship is being transferred to Virginia from another jurisdiction.[37]

A Virginia court may decline to exercise jurisdiction if it determines, based on all relevant factors, that another state is a more appropriate forum. These factors include the adult's preferences, location and financial considerations, "nature and location of the evidence," where the adult's time is spent, and the court's familiarity with the facts and issues and ability to decide expeditiously, to protect the adult from abuse, neglect, or exploitation, and monitor the fiduciary's conduct.[38] The court may also decline to exercise jurisdiction if it finds that the person seeking the order has engaged in unjustifiable conduct.[39]

2. Transfer of Authority

The Act provides procedures for transferring an adult guardianship or conservatorship into or out of Virginia.[40] A Virginia court will issue an order provisionally transferring a guardianship or conservatorship to another jurisdiction where the adult or property is, or is reasonably expected to be present, if the court is satisfied that: (i) the arrangement will be accepted by the court in the other state, (ii) the transfer would not be contrary to the adult's interests, and (iii) proper arrangements have been made for the adult's care or the property's management.[41] The court will issue a final order upon confirmation that the court to which the proceeding is being transferred has accepted it.[42] A Virginia court will accept the transfer of a guardianship or conservatorship from another jurisdiction upon receipt of the other state's provisional order transferring the arrangement to Virginia, unless a party es-

36. *Id.* § 37.2-1039(3) (Repl. Vol. 2011).
37. *Id.* § 37.2-1040(a) (Repl. Vol. 2011).
38. *Id.* § 37.2-1042 (Repl. Vol. 2011).
39. *Id.* § 37.2-1043(a)(1) (Repl. Vol. 2011).
40. *See id.* § 37.2-1046 (Repl. Vol. 2011).
41. *Id.* § 37.2-1046(d), (e) (Repl. Vol. 2011).
42. *Id.* § 37.2-1046(f) (Repl. Vol. 2011).

tablishes that the transfer would be contrary to the interests of the adult, or the proposed guardian or conservator is ineligible for appointment in Virginia.[43]

3. Recognition of Orders from Other States

Guardians or conservators appointed by a court in another state may register in Virginia and exercise all powers not prohibited under Virginia law, including maintaining actions and proceedings here.[44]

D. *Successor Trustees for Land Trusts*

By amendment to Virginia Code section 55-17.1, the beneficiaries of a land trust shall name a successor trustee when the trustee named in the deed conveying property to the land trust "declines to serve, resigns, is disqualified or removed, or is adjudicated incapacitated" and the deed does not name a successor trustee.[45] The beneficiaries must act by majority decision.[46] If a majority cannot agree or if the beneficiaries cannot be identified from the recorded deed, the circuit court of the jurisdiction where the deed was recorded may appoint a successor trustee if it considers the appointment necessary for trust administration.[47] Any party interested in the trust's administration may move for appointment of a successor.[48]

E. *Out-of-State Institutions as Trustees*

In 2003, then Attorney General Jerry Kilgore opined that the federal National Bank Act preempted Virginia Code sections 6.2-1001 and 6.2-1014 to the extent that those state statutes purported to bar an out-of-state national bank, supervised and regulated by the Comptroller of the Currency, from engaging in trust busi-

43. *Id.* § 37.2-1047 (Repl. Vol. 2011).
44. *Id.* §§ 37.2-1048 to -1050 (Repl. Vol. 2011).
45. Act of Mar. 26, 2011, ch. 661, 2011 Va. Acts ___ (codified as amended at VA. CODE. ANN. § 55-17.1 (Cum. Supp. 2011)).
46. *Id.*
47. *Id.*
48. *Id.*

ness in Virginia if it does not have an office here.[49] The Virginia Code, however, continued to contain that prohibition.[50] The 2011 General Assembly codified the Attorney General's opinion by amending the two statutes to allow any national banking association to engage in the trust business in Virginia if it is regulated by the Comptroller of the Currency and authorized to act as a trustee, executor, administrator or any other fiduciary capacity in the commonwealth.[51]

F. *Notary Conflicts of Interests*

Established Virginia law prohibits a notary from notarizing documents to which the notary or the notary's spouse is a party or "in which either has a direct beneficial interest."[52] A 2011 amendment further prohibits a notary from notarizing a document where the notary "is a signatory or is named in the document."[53] The amended statute continues to declare that a notary nominated as a fiduciary in a will is not disqualified "for that reason alone," but such a person would appear to be ineligible to notarize the document in any event by virtue of having been "named" in it.[54] The new prohibition also appears to apply to notaries who (or whose spouses) are named in trusts as trustees, in powers of attorney as agents, or in any document as a non-fiduciary, such as a trust protector, lawyer, accountant or investment advisor.[55]

A notary who violates the statute is guilty of notarial misconduct, which can subject the notary to liability for damages proximately caused by the violation.[56] A violation can also subject the notary's employer to civil liability if the notary was acting within the scope of his or her duties and the employer knew or reasonably should have known about the misconduct.[57] Nevertheless, the

49. *See* 2003 Op. Va. Att'y Gen. 12, 14.

50. *See* VA. CODE ANN. §§ 6.2-1-1001, -1014 (Repl. Vol. 2010).

51. Act of Mar. 14, 2011, ch. 67, 2011 Va. Acts ___ (codified as amended at VA. CODE ANN. §§ 6.2-1-1001, -1014 (Cum. Supp. 2011)).

52. *See* VA. CODE ANN. § 47.1-30 (Repl. Vol. 2009 & Cum. Supp. 2011).

53. Act of Mar. 28, 2011, ch. 746, 2011 Va. Acts ___ (codified as amended at VA. CODE ANN. § 47.1-30 (Cum. Supp. 2011)).

54. *See id.*

55. *See id*.

56. *See* VA. CODE ANN. §§ 47.1-26, -30 (Repl. Vol. 2009 & Cum. Supp. 2011).

57. *See id*. § 47.1-27 (Repl. Vol. 2009).

notarial act is not automatically void; rather, it is voidable in the court's discretion on the motion of any person injured by it.[58]

III. CASES

A. *Suit by Only One Co-Administrator; Joinder; Statute of Limitations*

In *Addison v. Jurgelsky*, the Supreme Court of Virginia considered whether a wrongful death suit brought by only one co-administrator was time-barred when the other co-administrator was not joined until after the statute of limitations expired.[59] The decedent's parents qualified as co-administrators of his estate, but only his father was listed as the plaintiff in a malpractice suit filed shortly before the limitations period expired.[60] After a challenge, the father amended the complaint to add the mother as a plaintiff, in her capacity as co-administrator.[61] The circuit court granted the defendants' motion to dismiss, finding that the amendment was filed outside the limitations period and that the statute of limitations was not tolled prior to the mother's joinder because an action by only one co-administrator was a nullity.[62]

On the administrators' appeal, the Supreme Court of Virginia first considered whether a single co-administrator can file a wrongful death action.[63] While the wrongful death statute allows filing by "the personal representative," the court construed that language to require "unity of action" by all persons holding that office.[64] Nevertheless, since only an administrator has standing to sue in this instance, the court found that the father, a co-administrator, was "not a plaintiff without statutory authority to act."[65] It distinguished the present situation from prior opinions which had refused to allow a suit to continue when: (i) the original plaintiff had no standing to sue, either alone or with others,

58. *See id*. § 47.1-30 (Repl. Vol. 2009 & Cum. Supp. 2011).
59. 281 Va. 205, 207, 704 S.E.2d 402, 403 (2011).
60. *Id*.
61. *Id*., 704 S.E.2d at 404.
62. *Id*. at 207–08, 704 S.E.2d at 404.
63. *Id*. at 208, 704 S.E.2d at 404.
64. *Id*.
65. *Id*. at 209, 704 S.E.2d at 404–05 (citing VA. CODE ANN. § 8.01-50(B) (Repl. Vol. 2007)).

and an entirely new plaintiff would have had to be substituted;[66] or (ii) a new defendant would have had to be added after the expiration of the limitations period.[67]

The court pointed out that Virginia Code section 8.01-5(A) allows new parties to be added and misjoined parties dropped "at any time as the ends of justice may require."[68] It observed that in the instant case the absent necessary party was a plaintiff who, unlike a defendant, would not resist joinder.[69] Therefore, allowing the joinder would not be inconsistent with the public policy behind statutes of limitations, "to protect non-parties from becoming subject to judicial claims when the passage of time may have increased the difficulty of defending such claims."[70]

The court then held that the original filing effectively tolled the statute of limitations and the co-administrator could be joined because the other co-administrator was already a party and the underlying claims were unchanged.[71]

B. *Uniform Transfers to Minors Act: Custodian's Duty of Care and Remedies*

In *Carlson v. Wells*, Jon and his brother James were custodians of several accounts for Jon's children under the Virginia Uniform Transfers to Minors Act ("UTMA").[72] One of the children asked to see the financial records for his account.[73] When the custodians failed to respond, the child filed a complaint seeking their removal as custodians of the UTMA accounts, a full accounting, compensatory and punitive damages, and attorneys' fees and costs.[74]

66. *Id*. at 209–10, 704 S.E.2d at 405 (citing Cook v. Radford Cmty. Hosp., Inc., 260 Va. 443, 451, 537 S.E.2d 906, 910 (2000)).

67. *Id*. at 210–11, 704 S.E.2d at 405 (citing Ahari v. Morrison, 275 Va. 92, 96, 654 S.E.2d 891, 893–94 (2008); Mendenhall v. Douglas L. Cooper, Inc., 239 Va. 71, 75, 387 S.E.2d 468, 470 (1990)).

68. *Id*. at 210, 704 S.E.2d at 405 (quoting VA. CODE ANN. § 8.01-5(A) (Repl. Vol. 2007)).

69. *Id*. at 211, 704 S.E.2d at 405.

70. *Id*.

71. *Id*., 704 S.E.2d at 406.

72. 281 Va. 173, 177–78, 705 S.E.2d 101, 102–03 (2011).

73. *Id*. at 178, 705 S.E.2d at 103.

74. *Id*.

In response to the complaint, Jon provided a full accounting of the UTMA accounts and paid the children an amount he claimed was the entire balance in their accounts.[75] The accounting showed, however, that Jon had closed the individual UTMA accounts and transferred the balances to a single joint savings account in his and their names.[76] He had withdrawn funds from the combined account to reimburse himself for expenses he claimed were incurred on the children's behalf and "to make further investments."[77] He had transferred some funds to his personal investment accounts and used a combination of his own and the former UTMA funds to buy U.S. Airways stock shortly before the company declared bankruptcy.[78] The children brought suit for breach of fiduciary duty under the Virginia UTMA statute.[79]

The circuit court found that both custodians had breached their duties—James, by "abdicat[ing] his custodial responsibility," and Jon, "by failing to keep proper records" and speculating in risky stocks.[80] It assessed damages against James and Jon in proportion to the amounts in their custody and awarded the children attorneys' fees and related costs.[81] It did not order their removal as custodians because both had already resigned.[82]

On the custodians' appeal, the Supreme Court of Virginia first examined the applicable standard of care under former Virginia Code section 31-48, which was in effect during the time at issue.[83] The court found that the statute, prior to the 2007 amendment, applied "the standard of care that would be observed by a prudent person dealing with such person's own property."[84] The court declared that this language invoked the common-law "prudent person" standard, which required custodians "to use reasonable care and skill to preserve the UTMA funds,"[85] rather than the more demanding "prudent investor rule" made applicable to many oth-

75. *Id.*
76. *Id.*
77. *Id.*
78. *Id.* at 178–79, 705 S.E.2d at 103.
79. *See id.* at 178–79, 705 S.E.2d at 103.
80. *Id.* at 179–80, 705 S.E.2d at 104.
81. *Id.* at 180, 705 S.E.2d at 104.
82. *See id.* at 178, 705 S.E.2d at 103.
83. *Id.* at 180–81, 705 S.E.2d at 104 (citing VA. CODE ANN. § 31-48 (Repl. Vol. 2001)).
84. *Id.* at 181, 705 S.E.2d at 104 (quoting VA. CODE ANN. § 31-48 (Repl. Vol. 2001)).
85. *Id.* at 182, 705 S.E.2d at 105 (quoting RESTATEMENT (SECOND) OF TRUSTS § 176 (1959)).

er fiduciaries in 1999 by the Virginia Uniform Prudent Investor Act.[86] Nevertheless, the court held that the custodians' speculative investment in U.S. Airways stock was not proper under the prudent person standard, even if Jon (presumably a prudent person) had also invested his own funds in the same manner, because he was aware of the risk and did not make preservation of the custodial funds a primary consideration.[87]

The custodians attempted to escape liability for the losses incurred from the speculative investments by arguing that the overall performance of the children's investment portfolios had been positive.[88] This "portfolio" standard, embodied in the Uniform Prudent Investor Act and the current version of UTMA, permits some speculative investments.[89] The court held, however, that the prudent person rule that applied to UTMA custodians at the time of Jon and James' actions required evaluation of each investment in isolation and prohibited speculation.[90]

The court further observed that the custodians had a statutory duty to keep records of their transactions and therefore held that they bore the burden of untangling matters when their commingling of custodial and personal funds prevented a precise accounting.[91] It found that Jon and James had not met that burden and therefore upheld the lower court's award of compensatory damages with respect to the unaccounted funds.[92]

On the custodians' claim that they were entitled to attorneys' fees as prevailing parties, the court noted that James abdicated his duties, Jon commingled funds, they both refused to provide an accounting, and they generally misunderstood or ignored their re-

86. *See id.* at 184, 705 S.E.2d at 107; *see also* VA. CODE ANN. §§ 26-45.3 to -45.13 (Repl. Vol. 2011) (applying the prudent investor rule to a "trustee who invests and manages trust assets"). The 1999 Uniform Prudent Investor Act defines "trustee" in section 26-45.13 in part by incorporating the definition of "fiduciary" found in section 8.01-2. VA. CODE ANN. § 26-45.13 (Repl. Vol. 2001). Unfortunately, that section did not include "custodian" among the several different types of fiduciaries listed. *Id.* The General Assembly extended the Prudent Investor Act standards to custodians in 2007. *See* Act of Mar. 19, 2007, ch. 517, 2007 Va. Acts 704, 705 (codified as amended at VA. CODE ANN. § 26-45.13 (Repl. Vol. 2011)).

87. *Carlson*, 281 Va. at 182–83, 705 S.E.2d at 105–06.

88. *Id.* at 183, 705 S.E.2d at 106.

89. *See* VA. CODE ANN. § 26-45.4 (Repl. Vol. 2011); *id.* § 31-48 (Repl. Vol. 2011).

90. *Carlson*, 281 Va. at 183–84, 705 S.E.2d at 106.

91. *Id.* at 185–86, 705 S.E.2d at 107–08.

92. *See id.* at 186, 705 S.E.2d at 108.

sponsibilities.[93] It also noted that as a result of the suit, the plaintiffs, not the defendants, received all of the relief they requested except punitive damages.[94] While Virginia law generally does not allow courts to award attorneys' fees to prevailing parties, the court found that not only were the custodians not entitled to their attorneys' fees, but that their callous disregard of their custodial obligations and their "pervasive, wanton dereliction" of duties justified a fee award to the children.[95]

C. *Testamentary Capacity of Disabled Adult*

In *Parish v. Parish*, the Supreme Court of Virginia considered whether a testator with appointed conservators had testamentary capacity and whether a presumption of undue influence arose where the conservator was a major beneficiary under the testator's will and acted as his translator during the drafting process.[96]

Eugene suffered a debilitating injury while living in Florida, and a court there appointed a guardian for him.[97] He later moved to a Tennessee facility; there, his brother and sister-in-law were appointed co-conservators by a court.[98] He spent his final years in Virginia, with his son and daughter-in-law serving as conservators.[99]

While in Tennessee, Eugene executed a will leaving 50% of his estate to his brother and sister-in-law, who were his conservators, 25% to his son, and 25% to other family members.[100] It appointed his brother and sister-in-law as personal representatives.[101] Eu-

93. *Id*. at 187, 705 S.E.2d at 108.

94. *Id*. at 188, 705 S.E.2d at 109.

95. *Id*. at 188–90, 705 S.E.2d at 109–10.

96. 281 Va. 191, 194, 704 S.E.2d 99, 101 (2011).

97. *Id*. The applicable Florida statute required the court to find that he was "incapable of caring for himself or managing his property or . . . likely to dissipate or lose his property or inflict harm on himself or others." *Id*. (quoting FLA. STAT. § 744.331 (1989)).

98. *Id*. at 195, 704 S.E.2d at 101–02. The applicable Tennessee statute required the court to find that he was "in need of partial or full supervision, protection and assistance by reason of mental illness, physical illness or injury, developmental disability or other mental or physical incapacity." *Id*. (quoting TENN. CODE ANN. § 34-1-101(7) (2000)).

99. *See id*. at 196, 704 S.E.2d at 102. They were appointed after a Virginia court found that he was "incapacitated to such an extent that he [was] unable to care for himself, make medical decisions, manage his estate or understand his debts as they come due." 281 Va. at 196, 704 S.E.2d at 102 (internal quotation marks omitted).

100. *Id*. at 195–96, 704 S.E.2d at 102.

101. *See id*. at 196, 704 S.E.2d at 102.

gene's brother assisted in the will preparation process, acting as translator because the paralegal drafting the will had difficulty understanding Eugene.[102] He also was in the room when Eugene executed the will.[103] The Tennessee conservators did not tell Eugene's son about the will.[104]

After Eugene's death, his son qualified as administrator in Virginia, but the sister-in-law then presented the Tennessee will and sought appointment as executor.[105] The son filed a counterclaim to impeach the will, alleging that Eugene "lacked testamentary capacity" and "was subjected to undue influence."[106] The trial court found for the sister-in-law.[107]

On the son's appeal, the court first pointed to its previous holdings that the appointment of a guardian does not automatically deprive the ward of power to make a will.[108] It also noted that a lesser degree of capacity is required to make a will than to execute contracts or transact ordinary business.[109] It reiterated that a testator must be "capable of recollecting [his] property, the natural objects of [his] bounty and their claims upon [him and know] the business about which [he] was engaged and how [he] wished to dispose of [his] property."[110] It observed that none of the three statutes that had governed Eugene's conservatorships required a specific finding that he was so incompetent as to be unable to execute a will.[111] Accordingly, no presumption of incapacity arose.[112]

The court next noted that because Eugene's son did not question the execution of the will, his sister-in-law was entitled to a presumption that Eugene had testamentary capacity when he signed it, and the son had to produce evidence sufficient to rebut the presumption.[113] The son produced only his own testimony and

102. *Id.* at 195, 704 S.E.2d at 102.
103. *Id.*
104. *Id.* at 196, 704 S.E.2d at 102.
105. *Id.*
106. *Id.* at 196–97, 704 S.E.2d at 102.
107. *Id.* at 197, 704 S.E. 2d at 102.
108. *Id.*, 704 S.E.2d at 103 (quoting Gilmer v. Brown, 186 Va. 630, 637, 44 S.E.2d 16, 19 (1947)).
109. *Id.* at 198, 704 S.E.2d at 103 (quoting *Gilmer*, 186 Va. at 637, 44 S.E.2d at 19).
110. *Id.* (quoting Thomason v. Carlton, 221 Va. 845, 852, 276 S.E.2d 171, 175 (1981)).
111. *Id.* at 199, 704 S.E.2d at 104.
112. *Id.*
113. *Id.*

the testimony of his wife and a physician who had examined Eugene more than two years after the will was executed.[114] The court noted, however, that the time of signing is the critical time for determining testamentary capacity and that great weight should be given to the testimony of the drafter, the witnesses, and attending physicians.[115] The drafter and witnesses testified that they thought Eugene knew what he was doing, and the physician who was treating him at that time testified "with a reasonable degree of medical probability that Eugene could understand what property he owned and to whom he was giving it."[116] Eugene's brother, sister-in-law, social worker, and another attorney all supported the contention that Eugene was not capable of executing a will.[117] The court therefore ruled that the circuit court had sufficient evidence to find that Eugene had testamentary capacity.[118]

In considering the allegation of undue influence, the court noted that, while its previous opinions dealt with persons of advanced age, the principles they set forth are "equally applicable to [all] testators who have weakness of mind, whether from injury. . . or from any other causes."[119] When such a person "has named a beneficiary with whom [he] stood in a relationship of confidence or dependence, and when [he] previously had expressed [either] a contrary intention or . . . no intention about disposition of his property, a presumption of undue influence arises."[120] The burden of producing evidence to rebut the presumption then shifts to the proponent of the will.[121] In this instance, it appeared that the sister-in-law had produced evidence that Eugene was not unduly influenced, as the circuit court had found by clear and convincing evidence—"a higher standard than required."[122] The court therefore affirmed that ruling.[123]

114. *See id*. at 200, 704 S.E.2d at 104.
115. *Id*., 704 S.E.2d at 104–05 (citations omitted).
116. *Id*. at 200–01, 704 S.E.2d at 105.
117. *Id*. at 201, 704 S.E.2d at 105.
118. *Id*. at 202, 704 S.E.2d at 105.
119. *Id*., 704 S.E.2d at 106.
120. *Id*.
121. *Id*. at 203, 704 S.E.2d at 106 (quoting Martin v. Phillips, 235 Va. 523, 529, 369 S.E.2d 397, 400 (1988)).
122. *Id*. at 204, 704 S.E.2d at 102, 106.
123. *Id*.

D. *Estate's Liability for Debt on Survivorship Property*

In *Dolby v. Dolby*, the Supreme Court of Virginia considered whether a decedent's estate should be liable for a debt evidenced by a promissory note, executed by the decedent alone, but secured by a deed of trust on real estate held as tenants by the entirety.[124] The decedent bought a house and executed a promissory note secured by the property.[125] He later married and transferred the property into a tenancy by the entirety, but his wife did not assume the obligation or become a joint obligor on the note.[126] His will directed payment of all legally enforceable debts except those secured by property he owned at his death.[127] His executors sought "aid and direction" as to whether the estate was liable for the debt or whether instead his widow should take the property subject to it.[128] The circuit court held that the debt was not the estate's obligation.[129]

On appeal by the widow, the court first considered whether the decedent had a personal obligation to pay the debt.[130] It found that the debt was originally his and that nothing subsequent to his marriage had changed that status.[131]

The court next considered whether the debt was secured by real estate he owned at his death, which would qualify it for the testamentary exception to his direction to pay all legally enforceable debts.[132] It found that his "ownership interest did not survive his death," instead "pass[ing] to his [widow] by operation of law."[133] Because the interest was not part of his probate estate, he could not charge his debts against it.[134] Thus his estate, and not his widow, was liable for the debt.[135]

124. 280 Va. 132, 134, 694 S.E.2d 635, 636 (2010).
125. *Id*.
126. *Id*.
127. *Id*.
128. *Id*. at 135, 694 S.E.2d at 636.
129. *Id*.
130. *Id*. at 135–36, 694 S.E.2d at 636–37.
131. *See id*. at 136, 694 S.E.2d at 637.
132. *See id*. at 136–37, 694 S.E.2d at 637.
133. *Id*. at 137, 694 S.E.2d at 637.
134. *See id*. at 137, 694 S.E.2d at 637–38 (citing Edmunds v. Scott, 78 Va. 720, 726 (1884)).
135. *See id*., 694 S.E.2d at 638.

E. *Adverse Possession by Co-Tenant*

In *Harkleroad v. Linkous*, the Supreme Court of Virginia considered whether a co-tenant with an undivided one-half interest in residential property could show adverse possession against the other co-tenants so as to obtain fee title to the entire property.[136]

A widow owned a one-half interest in her residence, and relatives owned the other half subject to her life estate; but she executed a deed purporting to convey the property to an unrelated buyer in fee simple.[137] Eight years later, the Linkouses purchased the buyer's interest at a tax sale.[138] They renovated the dwelling and rented it for sixteen years.[139] When a prospective purchaser questioned their ownership interest, they brought a quiet title action asserting ownership through adverse possession.[140] The relatives cross-claimed for an accounting of rents and a partition of the property.[141]

The relatives admitted that the Linkouses had been in "actual, exclusive, visible and continuous possession" of the property for at least the fifteen-year period required for adverse possession under Virginia Code section 8.01-236.[142] They argued, however, that the possession had not been "hostile" because the Linkouses were not aware of the relatives' claim to a one-half interest.[143] The court observed that "there is a presumption against any occupancy of a co-tenant being hostile . . . to others . . . with whom he is in privity."[144] The presumption does not apply, however, where strangers to the original co-tenancy, who are not in privity with the other co-tenants, take possession through a conveyance that "purports to give them the right to possess the whole property and [they] claim[] ownership of the whole."[145] Here, the Linkouses, who were not in privity with the relatives, did not need to discov-

136. 281 Va. 12, 15, 704 S.E.2d 381, 381 (2011).
137. *Id.* at 15–16, 704 S.E.2d at 382.
138. *Id.* at 16, 704 S.E.2d at 382.
139. *Id.*
140. *Id.*, 704 S.E.2d at 382–83.
141. *Id.*, 704 S.E.2d at 383.
142. *Id.* at 18, 704 S.E.2d at 384; *see* VA. CODE ANN. § 8.01-236 (Repl. Vol. 2007 & Cum. Supp. 2011).
143. *Harkleroad*, 281 Va. at 17, 704 S.E.2d at 383.
144. *Id.* at 18, 704 S.E.2d at 384 (citations omitted).
145. *Id.* at 19, 704 S.E.2d at 384 (citing Shenandoah Nat'l Bank v. Burner, 166 Va. 590, 593, 186 S.E. 92, 93 (1936)).

er the relatives' co-tenancy and give them actual notice of the Linkouses' claim.[146] Their actions were so open and obvious as to provide constructive notice of their intent to oust the relatives.[147]

On its own motion, the court noted that the widow's deed arguably did not convey her life interest and that the record did not show when she died.[148] Adverse possession generally does not begin to run against a remainderman until the life tenant's death because the "remainderman has no right to eject the adverse possessor" during the life tenancy.[149] In this instance, however, the relatives had not raised the issue at trial or on appeal, so the court assumed they had agreed that the fifteen-year period began to run against their interests when the Linkouses took exclusive possession of the property, even if the widow was still alive.[150]

F. *Powers of Attorney-in-Fact*

In *Smith v. Mountjoy*, the Supreme Court of Virginia considered whether transactions by an agent under a durable power of attorney exceeded her authority and, if so, whether the principal nevertheless ratified them.[151]

Using her husband's durable general power of attorney, the wife created a trust for him and conveyed to herself, as trustee of the trust, a one-half interest in real estate they had held as tenants by the entirety.[152] She conveyed the other one-half interest to a separate trust she created for herself on the same day.[153] The husband's trust was to distribute the assets remaining at his death to the wife or, if she did not survive, to other beneficiaries.[154] In contrast, the wife's trust gave the husband only an income interest and a right to principal necessary for his "support, maintenance and medical care," with the remainder passing at

146. *Id.*
147. *Id.*
148. *Id.* at 20–22, 704 S.E.2d at 385–86.
149. *See id.* at 21, 704 S.E.2d at 385.
150. *See id.* at 22, 704 S.E.2d at 386.
151. 280 Va. 46, 48–49, 694 S.E.2d 598, 599 (2010).
152. *Id.* at 49–50, 694 S.E.2d at 599–600.
153. *Id.*, 694 S.E.2d at 600.
154. *Id.* at 49, 694 S.E.2d at 600.

his death to the same contingent beneficiaries.[155] The husband was not informed of these transactions.[156]

When the husband learned of these actions after the wife's death, he executed a "Notice of Termination. . . to revoke and terminate his trust."[157] He sought a judicial declaration that the wife had exceeded her authority by creating his trust and conveying their entire property to the two trusts, and that he was the sole owner of the one-half interest held by the wife's trust.[158] He also made a written demand for all of the income of the wife's trust and substantial principal to defray his medical expenses.[159] After his death, the circuit court partially granted his executor's motion for summary judgment, finding that the transactions were gifts not authorized by the power of attorney and that the husband had not ratified them by his later actions.[160]

On appeal, the wife's trustee argued that the transfers were not gifts because the husband (through his attorney-in-fact) and wife had each given up property rights in return for equivalent rights in the other's property interest.[161] The court rejected that argument, holding that the differing terms of the two trusts "conferred a benefit [on the wife] that she did not have when the properties were held as tenants by the entirety," with "no corresponding benefit" to the husband.[162] The net result was a gift to the wife, which was not authorized by the terms of the husband's power of attorney.[163]

The wife's trustee next argued that the husband ratified the transactions by following the procedure specified in his trust agreement to terminate that trust and by demanding distributions from the wife's trust.[164] The court found, however, that the husband, after learning of the wife's actions, promptly disavowed them by terminating his trust and filing suit to undo her sever-

155. *Id*. at 49–50, 694 S.E.2d at 600.
156. *Id*. at 50, 694 S.E.2d at 600.
157. *Id*. (internal quotation marks omitted).
158. *Id*.
159. *See id*. at 50–51, 694 S.E.2d at 600.
160. *Id*. at 51–52, 694 S.E.2d at 601.
161. *Id*. at 53, 694 S.E.2d at 602.
162. *Id*. at 54, 694 S.E. at 602–03.
163. *See id*., 694 S.E.2d at 603.
164. *Id*. at 56, 694 S.E.2d at 604.

ance of their property interests.[165] It also noted that his demand for income and principal from the wife's trust was not inconsistent with his challenge to her actions as attorney-in-fact, since her trust contained assets other than the properties at issue.[166]

G. *Trust Division and Termination at Beneficiaries' Request*

In *Ladysmith Rescue Squad, Inc. v. Newlin*, the Supreme Court of Virginia considered whether a circuit court should have divided and partially commuted a testamentary charitable remainder unitrust over a charitable beneficiary's objection.[167] The decedent's will directed the trustee to pay a unitrust amount to individual beneficiaries for life and then to distribute the remainder equally to two charities.[168] The will authorized the trustees to amend the trust in any manner necessary to preserve its federal tax qualification.[169] It also contained a spendthrift clause prohibiting the beneficiaries from encumbering or otherwise controlling their shares until actually paid to them.[170] On the petition of the income beneficiaries and one of the two charities, however, the circuit court authorized the trustees to divide the unitrust into two equal trusts and to distribute the actuarial values of the petitioners' interests in one of the trusts to them immediately.[171]

On appeal by the other charity, the court noted that the will did not expressly authorize a division or commutation.[172] Accordingly, to authorize division, the beneficiaries relied on Virginia Code section 55-544.17, the provision of the Uniform Trust Code ("UTC") that allows a trustee to divide a trust if the result does not "materially impair the rights of any beneficiary or adversely affect achievement of the purposes of the trust."[173] For authority to commute and terminate the divided trust, they relied on section 55-544.12(A), the UTC provision that allows for a modifica-

165. *Id.* at 56–57, 694 S.E.2d at 604.
166. *Id.* at 57, 694 S.E.2d at 604.
167. 280 Va. 195, 198, 694 S.E.2d 604, 606 (2010).
168. *Id.*
169. *See id.* at 200–01, 694 S.E.2d at 607.
170. *Id.* at 198, 694 S.E.2d at 606.
171. *Id.* at 199–200, 694 S.E.2d at 606–07.
172. *Id.* at 200–01, 604 S.E.2d at 607.
173. *Id.* (quoting VA. CODE ANN. § 55-544.17 (Repl. Vol. 2007 & Cum. Supp. 2011)).

tion or termination that, due to circumstances not anticipated by the settlor, would further the trust purposes.[174]

The court declared that the UTC did not alter the fundamental principles of will construction that: (i) the "testator's or settlor's intent prevails over the desires of the beneficiaries," and (ii) "intent is to be ascertained the language the testator or settlor used."[175] Unless a trust has been mismanaged, become uneconomic, or has objects that have become unobtainable, the UTC allows termination only in "circumstances not anticipated by the settlor."[176] Here, the court found nothing in the record to indicate that the settlor had not anticipated that the beneficiaries might want the value of their interests sooner.[177] Rather, it found that the settlor's purposes included providing an income stream for the individual beneficiaries "while shield[ing] [it] from their creditors and from their own interference."[178] Dividing the unitrust and terminating one of the resulting trusts would completely frustrate those purposes.[179]

The court also found that even dividing the unitrust was impermissible because the division was merely a device for securing a prepayment of the petitioners' interests without having to seek the approval of the other charity, the only party purporting to defend the settlor's interest.[180]

H. *Waiver of Prudent Investor Rule: Duty to Warn Beneficiaries Regarding Corporate Trustee's Stock, Duty of Co-Trustee to Seek Court's Aid and Guidance, and Enforceability of Nonjudicial Settlement Agreements*

A recent federal case, *W.A.K. ex rel Karo v. Wachovia Bank, N.A.*, also addressed several issues of Virginia law of particular interest to corporate fiduciaries.[181]

174. *Id.* (citing VA. CODE ANN. § 55-544.12(A) (Repl. Vol. 2007 & Cum. Supp. 2011)).
175. *Id.* at 201–02, 694 S.E.2d at 608.
176. *See id.* at 202, 694 S.E.2d at 608 (quoting VA. CODE ANN. § 55-544.12(A) (Repl. Vol. 2007 & Cum. Supp. 2011)).
177. *See id.*
178. *Id.* at 202–03, 694 S.E.2d at 608–09.
179. *Id.* at 203, 694 S.E.2d at 609.
180. *See id.*
181. 712 F. Supp. 2d 476 (E.D. Va. 2010), *appeal denied*, No. 10-2023 (4th Cir. Mar. 31, 2011), *and rehearing denied*, No. 10-2023 (4th Cir. May 10, 2011).

The grantor created a revocable trust in 1966 with her husband Toney and Central National Bank ("CNB") as co-trustees, funding it primarily with CNB stock.[182] The grantor's father was a founder of the bank, and for many years it had been considered a family business.[183] She gave her trustees "uncontrolled discretion" over the investment of the trust assets, including the ability "to retain as permanent any now existing investments (including stock of the corporate [t]rustee or in any of its affiliates and holding companies) of the trust property" and "invest the trust property . . . without being confined to investments lawful through statute or otherwise for fiduciaries in the State of Virginia."[184] The [t]rustees were expressly authorized to invest "as they in their uncontrolled discretion may deem advisable . . . including . . . stock in the corporate [t]rustee or in any of its affiliates and holding companies."[185] Wachovia Bank, N.A. later succeeded CNB as co-trustee through a series of mergers.[186]

At the grantor's death in 1974, Toney became the sole income beneficiary.[187] The trust also provided the corporate trustee the power to make discretionary principal distributions to the grantor, and Toney's son Drew and Drew's minor son W.A.K., which the trustees exercised on several occasions.[188]

Wachovia contended that, between 2003 and 2007, it repeatedly warned Toney and Drew of the possible risks associated with the trust's continued investment concentration in bank stock and recommended diversification.[189] The co-trustee and beneficiaries rejected this advice, and as of late 2007, Wachovia stock still made up approximately 65% of the trust's assets.[190] Although one may only speculate as to the family's true reasoning, it is possible

182. *Id.* at 479.

183. Defendant-Appellee's Motion to Dismiss Appeal as Not Within the Jurisdiction of the Court at 2–3, W.A.K. *ex rel.* Karo v. Wachovia Bank, N.A., No. 10-2023 (4th Cir. Oct. 18, 2010) [hereinafter Defendant's Motion to Dismiss Appeal].

184. *W.A.K.*, 712 F. Supp. 2d at 481.

185. *Id.*

186. *Id.* at 479.

187. Wachovia Bank, N.A.'s Memorandum of Law in Support of It's Motion to Dismissal Counts of the Complaint Pursuant to Fed. R. Civ. P. 12(b)(6) at 2, W.A.K. *ex rel.* Karo v. Wachovia Bank, N.A., 712 F. Supp. 2d 476 (E.D. Va. 2010) (No. 3:09-cv-00575-HEH) [hereinafter Wachovia's Memorandum of Law].

188. *Id.*

189. *See W.A.K.*, 712 F. Supp. 2d at 480.

190. *Id.* at 479–80.

that Toney and Drew did not wish to diversify in part because of the family's long personal connection to the bank, the historically generous dividends paid by the bank, and the significant capital gains that would have been realized upon any sale.[191]

In the face of its co-trustee's repeated refusal to diversify, Wachovia obtained "letters of retention" from both Toney and Drew, acknowledging the bank's advice regarding the benefits of diversification, directing Wachovia to maintain the existing concentration, and releasing and indemnifying it against any resulting liability.[192] Shortly after the latest letter was signed in 2007, the U.S. economy entered the worst recession since the Great Depression, and bank dividends and share prices declined precipitously.[193]

Acting as his father's attorney-in-fact in August 2008, Drew unsuccessfully attempted to disclaim his father's income interest and thereby claim the trust assets as the remainder beneficiary.[194] In January 2009, the Richmond Circuit Court granted the parties' request to modify the trust to allow principal distributions for Toney's needs if the trust income was not sufficient.[195] At Drew's request, the court's order also added a spendthrift provision to the trust.[196] Three weeks later, Drew attempted to disclaim his own contingent remainder interest in the trust, but retained his right to receive discretionary principal distributions during Toney's lifetime.[197] Less than seven months later, his wife sued the corporate trustee on behalf of W.A.K., alleging, inter alia, that the bank had breached its fiduciary duty by maintaining the concentration of bank stock, notwithstanding the co-trustee's refusal to diversify and the beneficiaries' express wishes that the stock not be sold.[198]

191. *See id.* at 487 n.5 (referencing a witness's affidavit).

192. *Id.* at 482–83.

193. *See id.* at 480.

194. *See* Final Order, Karo v. Wachovia Bank, N.A., No. CL08-4650-4 (Richmond Circuit Court Jan. 25, 2009); Complaint at 2, Karo v. Wachovia Bank, N.A., No. CL08-4650-4 (Richmond Circuit Court Nov. 25, 2008).

195. Consent Order at 2, Karo v. Wachovia Bank, N.A., No. CL08-4650-4 (Richmond Circuit Court Jan. 1, 2009).

196. *Id.*

197. *W.A.K.*, 712 F. Supp. 2d at 480 n.1.

198. *See id.* at 480.

W.A.K. alleged that the trust language was insufficient to waive the prudent investor rule under Virginia law.[199] Therefore, he argued, Toney's refusal to consent to the diversification constituted a serious breach of trust that Wachovia, as co-trustee, had a duty under Virginia Code section 55-547.03(G) to redress by asking the court to compel diversification.[200] Alternatively, W.A.K. argued that the elderly Toney had effectively ceased to serve as a co-trustee at some point before 2008.[201] As a result, Wachovia allegedly had the unilateral power (and obligation) to reduce the concentration of bank stock notwithstanding Toney and Drew's wishes.[202] W.A.K. also contended that Wachovia's request that the beneficiaries sign the letters of retention was an impermissible attempt to protect the trustee from the consequences of what it knew to be an inadvisable course of action by shifting the fiduciary responsibility onto the beneficiaries.[203] Lastly, W.A.K. argued that the bank had a duty to monitor and warn the beneficiaries specifically about the declining value of its stock, which it failed to do.[204]

Wachovia moved for summary judgment, arguing that the trust language effectively waived the duty to diversify under Virginia law and that its reliance on that waiver was reasonable.[205] The district court agreed, holding that the bank had no duty to ask a court to compel diversification and could not be held liable for failing to do so.[206] It found that Toney, while a passive trustee, participated sufficiently in the ongoing administration of the trust so that the corporate trustee could not act unilaterally in the face of Toney's refusal to diversify.[207]

199. *See id*. at 480–82; *see also* Plaintiff's Memorandum of Law in Opposition to Wachovia Bank, N.A.'s Motion to Dismiss All Counts Pursuant to Pursuant Fed. R. Civ. P. 12(b)(6) at 15, W.A.K. *ex rel*. Karo v. Wachovia Bank, N.A., 712 F. Supp. 2d 476 (E.D. Va. 2010) (No. 309-cv-00575-HEH).

200. *See* Opening Brief of Appellant at 17, W.A.K. *ex rel.* Karo v. Wachovia Bank, N.A., No. 10-2023 (4th Cir. Nov. 12, 2010).

201. *W.A.K.*, 712 F. Supp. 2d at 484; *see also* Opening Brief of Appellant, *supra* note 200, at 8 (discussing Toney's "little interest" in serving as a trustee).

202. *W.A.K.*, 712 F. Supp. 2d at 484; *see also* VA. CODE ANN. § 55-547.03(D) (Repl. Vol. 2007) (discussing co-trustee responsibilities).

203. *See W.A.K.*, 712 F. Supp. 2d at 486.

204. *Id*. at 480, 487.

205. *See id*. at 481–82.

206. *See id*.

207. *Id*. at 484.

In rejecting W.A.K.'s claim that the bank had a duty to monitor and warn the beneficiaries about the performance of its stock specifically, the court noted that prohibitions against self-dealing and insider trading prevented the corporate fiduciary from giving advice regarding its own stock, and that a trustee could not be found to have breached one fiduciary duty because it failed to breach another.[208] It ruled that Wachovia had satisfied its duty of loyalty to the beneficiaries by alerting them to the potential conflict and encouraging them to seek outside advice regarding the Wachovia stock's suitability as an investment.[209]

The court also granted in part the bank's third-party motion for contribution from Drew, based on the letters of retention he signed, and its request for attorneys' fees from the trust under Virginia Code section 55-550.04.[210]

In an interesting coda to the case, Toney died after the district court's decision was entered, but before W.A.K.'s appeal could be heard.[211] As a result of Toney's death, Wachovia successfully argued to the Fourth Circuit Court of Appeals that Drew's attempted 2009 disclaimer was invalid[212] and that the spendthrift provi-

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208. *Id*. at 484–85.

209. *Id*. at 486.

210. W.A.K. *ex rel* Karo v. Wachovia Bank, N.A., No. 3:09-cv-575-HEH, 2010 U.S. Dist. LEXIS 72289, at *8–10 (E.D. Va. July 19, 2010).

211. *See id*. at *4.

212. *See* W.A.K. *ex rel*. Karo v. Wachovia Bank, N.A., No. 10-2023 (3:09-cv-00575-HEH) (4th Cir. Mar. 31, 2011). Based on the brief dismissal order, the reasons behind the court's belief that the disclaimer is invalid are not known. *See id.* However, Wachovia's pleadings set forth several alternative theories under which Drew's prior acceptance of trust benefits had made him ineligible to disclaim under Virginia Code section 64.1-196.12. Defendant-Appellee's Motion to Dismiss, *supra* note 183, at 11 (citing VA. CODE ANN. § 64.1-196 (Repl. Vol. 2007)) (stating that disclaimer is barred if, *inter alia,* disclaimant has accepted the interest or voluntarily assigned, conveyed, encumbered, pledged or transferred it). First, when Drew filed suit in Virginia state court in 2008 to uphold his attempted disclaimer of Toney's income interest and terminate the trust in favor of himself as the remainder beneficiary, Drew held himself out as the rightful owner of the property he later sought to disclaim. *Id.* at 4. This constituted an acceptance of the interest. Second, unlike situations where a beneficiary disclaims an income interest but retains a remainder interest (or vice versa), Drew's acceptance of principal distributions prevented him from disclaiming the corpus that would remain in the trust at Toney's death. *Id.* at 13–14. Third, if an interest has been encumbered or pledged by a beneficiary, it cannot later be disclaimed. *Id.* at 17 (quoting VA. CODE ANN. § 64.1-196.12(B)(ii) (Repl. Vol. 2007)). Drew had previously encumbered his remainder interested by borrowing amounts from the trust and signing the letters of retention by which he agreed to indemnify the trustee, both of which acts created an equitable lien against his beneficial interest under Virginia law. *Id.* at 17–18 (citing VA. CODE ANN. § 64.1-196.12(B)(iii) (Repl. Vol. 2007)). Finally, Drew's disclaimer was illusory because he purported to give up his remainder in-

sion previously added to the trust prevented the invalid disclaimer from operating as a transfer of Drew's remainder interest under Virginia Code section 64.1-196.12(F).[213] Therefore, because the trust remainder vested in Drew at Toney's death, the court held that W.A.K. no longer had standing as a trust beneficiary to pursue the appeal and dismissed it for lack of subject-matter jurisdiction.[214]

IV. CONCLUSION

Although the 2011 session of the Virginia General Assembly was a relatively quiet one in terms of wills, trusts, and estates, it did address several significant gaps in Virginia law and inconsistencies between Virginia and federal laws. In the process, however, the General Assembly departed from longstanding rules of construction by: (i) authorizing courts to consider extrinsic evidence to contradict the plain meaning of a formula funding clause in a will or trust, and (ii) allowing beneficiaries to agree among themselves to re-write the express funding provisions of a will or trust without any court involvement. Both actions were intended to address an unpredicted and retroactive change in the federal transfer tax laws for 2010 decedents, and thus the legislation was certainly well-intentional and limited to a very specific set of circumstances. Nevertheless the decision to exalt the wishes of the beneficiaries over the testator's intent, which traditionally has been the "pole star" governing will and trust interpretation, is troubling. It seems particularly incongruous with the rationale of the *Ladysmith Rescue Squad* case, where the Supreme Court of Virginia looked diligently for the testator's intent and upheld it despite the trustee's attempt to honor the contrary wishes of the

terest in the corpus while retaining the right to receive discretionary distributions of principal during Toney's lifetime. *Id.* at 18–19. Thus, he actually gave up nothing. *Id.* at 19. It is impossible to tell which of these grounds the court found convincing. However, the court had to have concluded that at least one constituted a bar to a valid disclaimer under Virginia law.

213. Defendant's Motion to Dismiss, *supra* note 183, at 19–20. Even if the spendthrift clause did not prohibit such a "transfer," Wachovia argued that the trust corpus first vested in Drew upon Toney's death before the transfer could be given effect. *Id.* (citing VA. CODE ANN. § 55.545.02(C) (Repl. Vol. 2007); Jackson v. Fid. & Deposit Co., 269 Va. 303, 312–13, 608 S.E.2d 901, 905–06 (2005)). Accordingly, any standing obtained by W.A.K. as a result of the transfer would have been merely derivative of Drew's, but W.A.K. litigated the case as an independent beneficiary and not as an assignee. *Id.* at 9.

214. *See* W.A.K. *ex rel.* Karo v. Wachovia Bank, N.A., No. 10-2023 (3:09-cv-00575-HEH) (4th Cir. Mar. 31, 2011).

beneficiaries. Now that the wall has been breached, it may be only a matter of time before other statutory exceptions to Virginia's traditional "four corners" doctrine follow.

The 2011 statutory amendments also created potential ambiguities in two other areas. First, in setting forth a method to appoint a successor trustee for a land trust under Virginia Code section 55-17.1 where the recorded deed does not provide for one, the General Assembly may have overlooked the fact that many trusts holding real estate are governed by a separate trust agreement that may include successor trustee provisions. Further legislative action is needed to clarify whether the successor trustee should be the person identified by the settlor or others pursuant to the agreement or the person selected by the majority of trust beneficiaries under the amended statute. In doing so, the authors posit that, once again, the settlor's intent should normally override the wishes of the beneficiaries.

Second, the General Assembly also created a possible ambiguity in the rules governing notaries. In addition to the existing prohibition against the notarization of any document to which the notary is a "party" or in which he or she has a "direct beneficial interest," the 2011 legislation prohibited a notary who is "named in a document" or is a "signatory" to it from notarizing that document. The statutory exception for notaries who are nominated as fiduciaries in a will, however, expressly applies only for purposes of determining whether the notary is deemed to be a party to or to have a direct beneficial interest in the will, it does not extend to a notary who may be "named" or a "signatory" in the document. Thus, it is not clear whether a notary who is nominated as a fiduciary (and thus is "named" in the will) is prohibited from acting under the statute, as amended. Viewing the fiduciary exception as applicable to the general rule ignores the express language of the statute. One might argue that what is notarized in connection with a will is a self-proving affidavit, which is not part of the will itself, and therefore the notary who is nominated as a fiduciary is not "named" in the document being notarized. Nevertheless, the fact that one nominated as a fiduciary is "named" in the will should counsel against having that person act as notary absent clarification of the notary conflict rules. The General Assembly could greatly assist practitioners by providing further guidance on this question in 2012.