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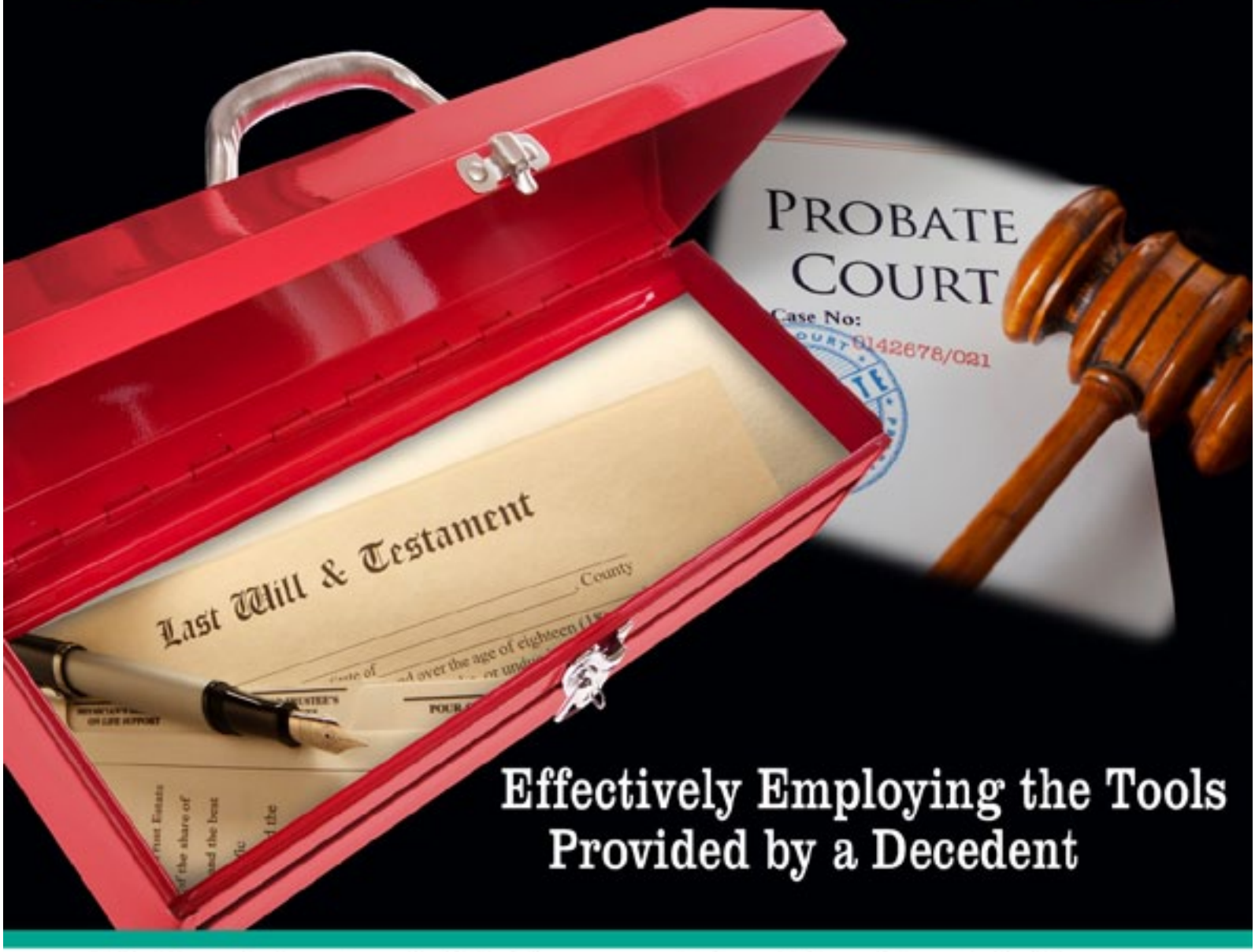

Effectively Employing the Tools Provided by a Decedent

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Effectively Employing the Tools Provided by a Decedent

By Ray Koenig, Ashley Kisner and Chris Hopkins

Anyone who has read a lengthy user agreement regularly employed by companies like Apple and Amazon knows that arbitration clauses in business and consumer contracts are now commonplace. Arbitration, a form of alternative dispute resolution where a neutral third party listens to both sides of a dispute and makes a binding decision, has long been used by large companies as an alternative to lengthy and binding lawsuits.

Recently, a greater frequency of estate plans are including mandatory arbitration provisions that require fiduciaries and beneficiaries to submit all disputes to arbitration. Similarly, no-contest clauses, which provide that beneficiaries who contest a provision of a will or trust forfeit any interest they may have in the estate or trust property, are more frequently being included and expanded to limit even further the benefi-

ciaries' ability to challenge estate planning documents. With the right counseling, fiduciaries acting under estate planning documents may be able to effectively employ mandatory arbitration clauses and expansive no-contest clauses to discourage beneficiaries from bringing lengthy and expensive lawsuits.

A mandatory arbitration clause in a will or trust usually provides that any dispute or controversy among the representatives/trustees and beneficiaries involving any aspect of the estate or trust is required to be submitted to binding arbitration. Compared to litigation, mandatory arbitration provides fiduciaries with certain advantages and disadvantages. Unlike judges in litigation who are likely to be randomly assigned to a case, in arbitration, the parties are usually able to select an arbitrator experienced and familiar with the subject matter.

If a decedent, however, selected a specific individual, type of person, or entity to serve as the arbitrator, the parties may find themselves in a precarious situation if the selected arbitrator is unavailable or otherwise unable to arbitrate the dispute. Despite a decedent's best efforts to select an appropriate arbitrator, fiduciaries may find themselves bound by a decision made by someone who lacks experience and familiarity with the type of dispute.

Unlike litigation which proceeds in a public forum and makes information available to the public, arbitration filings are generally not public and may help families keep certain details private. A drawback of arbitration, however, is that absent a showing of fraud, most arbitrations are not subject to the appeal process. Although the finality provided by arbitration may avoid the costs and delay of an appeal, without the potential for having their decision reviewed, arbitrators may not follow applicable law and instead reach a solution on an equitable basis.

A mandatory arbitration clause in a will or trust usually provides that any dispute or controversy among the representatives/ trustees and beneficiaries involving any aspect of the estate or trust is required to be submitted to binding arbitration.

Fiduciaries seeking to enforce a mandatory arbitration provision must also recognize that parties generally cannot be forced to arbitration without giving their prior consent. Because it is unlikely that the parties participated in the drafting of the estate planning documents, fiduciaries nominated or acting under estate planning documents should always seek guidance from experienced counsel regarding the enforceability of a particular mandatory arbitration clause. Because the inclusion of mandatory arbitration clauses in wills and trusts is a recent trend, the ability of fiduciaries to enforce these clauses has and will continue to be addressed by various courts and state legislatures.

In Arizona, the Court of Appeals ruled that mandatory arbitration clause is not enforceable because arbitration is a creature of contract and relationships that arise out of a trust are not contractual.[1] In response, the Arizona legislature enacted a statute that explicitly authorized a trust instrument to provide mandatory, exclusive, and reasonable procedures to resolve issues between the trustee and interested persons.[2]

In a recent California case, a beneficiary of a trust brought an action for financial elder abuse and removal against trustee-beneficiary; the Appellate Court affirmed the trial court's finding that the arbitration provision of the trust was unenforceable against a beneficiary who did not sign an arbitration agreement and was seeking to have the amended trust set aside. The Court also reaffirmed that the strong public policy in favor of arbitration does not extend to those who are not parties to an arbitration agreement.[3]

The Texas Supreme Court found an arbitration provision in a trust enforceable because the donor in-

tended for the benefits of his trust to come with the conditions he specified, and thus the Texas arbitration act's requirement of mutual assent was met. The Court found that a beneficiary, by attempting to enforce rights that would not exist without a trust, can manifest assent to all provisions of a trust, including a mandatory arbitration provision.[4]

Similar to a mandatory arbitration clause, fiduciaries should also be aware of provisions requiring the parties to participate in mediation prior to legal proceedings regarding an estate-planning document. The goal of mandatory mediation is normally to require the fiduciary and beneficiary to come together with the other parties to explore a resolution prior to embarking on costly arbitration and/or litigation. Unlike formal legal proceedings, mediation often occurs prior to the exchange of information and documents required by litigation and sometimes available in arbitration.

No-contest clauses are also tools seeking to avoid expensive public litigation. Proponents of expanded no-contest clauses suggest that they further strengthen the decedent's desires to prevent a challenge to its documents and discourage what may otherwise be frivolous litigation. Critics claim expanded no-contest clauses unnecessarily limit the rights of beneficiaries by providing a strong incentive not to challenge the actions of a fiduciary. Fiduciaries can employ these clauses to deter beneficiaries from challenging any applicable document and being forced to use estate/trust resources in defense.

No-contest clauses are not only being included in estate plans more frequently but they are also frequently drafted in a more comprehensive manner to expand the actions that would require the beneficiary to forfeit their interest. Recent no-contest clauses include actions beyond a direct challenge to a will or trust by expanding the definition of challenge to include asserting a claim against a decedent's estate for any purpose. Another way to increase the scope of the no-contest clause is to expand the subject matter to include challenges to the validity of transfer of assets outside of probate such as life insurance policies or beneficiary designations on bank and investment accounts. In that situation, a challenge to a beneficiary designation would require the beneficiary to forfeit any interest in the estate or trust property.

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In addition to expanding the types and items subject to no-contest clauses, recent estate plans have also expanded the definition of those who are deemed to have "challenged" the document. Recent no-contest clauses have included not only those who assert or file a direct challenge but also those who indirectly conspire with, or voluntarily assist any person in taking such action. An example of an expanded no-contest clause the authors recently encountered in their litigation practice follows:

"Notwithstanding anything herein to the contrary, in the event that any one or more persons shall (a) challenge in whole or in part the validity of my will, any codicil hereto, the aforementioned trust (including amendments thereto) or any trust created thereunder (the "Applicable Documents"), (b) assert any claim against my estate, or (c) contest or render inoperative in whole or in part (i) any trust (including any amended or restatement to any trust) created by me or by another for my benefit, (ii) any beneficiary designation under any document, plan or policy which I have executed, (iii) any transfer of assets which I have made during my lifetime, then for all purposes of this instrument, each such person and all descendants of such person (whenever born) shall be deemed to have died unmarried and intestate prior to my death. The term "challenge" shall include any attempt (except as required by law), direct or indirect, by

any person to oppose, contest or set aside any provision of any of the Applicable Documents, as well as the attempt to conspire with, or voluntarily assist, any person in taking such an action."

A common hybrid between mandatory arbitration and no-contest clauses are provisions providing that a disputing beneficiary who is deemed to have participated in the mediation or arbitration in bad faith forfeits any interest they may have in the estate or trust property. Fiduciaries should always be aware of the existence of no-contest clauses and take note of their scope to, in conjunction with fiduciary counsel, determine the most effective means to employ the clause to protect the decedent's intentions.

Arbitration clauses are no longer limited to something that is buried deep in user agreements that most of us accept without reading. Instead, the increase in both arbitration agreements and the expanded scope of no-contest clauses in estate planning documents provide fiduciaries with additional tools to employ a strategic defense to possible challenges by beneficiaries. Any nominated or acting fiduciary should at least be aware of their existence and consider consulting with experienced counsel for guidance.

1 *Schoneberger v. Oelze*, 208 Ariz. 591, 96 P.3d 1078 (Ariz. Ct. App. 2004)

2 ARIZ.REV.STAT.ANN. § 14-10205

3 *McArthur v. McArthur,* 224 Cal. App. 4th 651, 168 Cal. Rptr. 3d 785 (2014)

4 *Rachal v. Reitz*, 403 S.W.3d 840 (Tex. 2013)

Ray Koenig, Ashley Kisner and Chris Hopkins are key members of Clark Hill's national Trusts & Estates Controversy team. Kisner is based in Dallas, while Koenig and Hopkins are based in Chicago. Each has spent significant time throughout their careers advising and representing clients in trust and estate controversies. The authors are experienced litigators known by their clients and peers for their pragmatism, creativity, and responsiveness. Each is very involved in various professional communities, with Koenig being an ACTEC Fellow.