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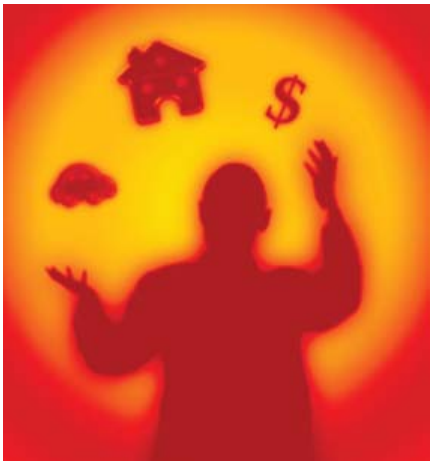

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Exoneration Clauses – Not All They're Cracked Up to Be

Intent is a paramount concern in construing the provisions of a will or trust, but public policy considerations often play an important role. While these concerns generally coincide, when matters of public policy conflict with a dispositive plan, public policy considerations will be decisive of the outcome.

Public policy concerns most often come into play when issues of fiduciary duty and liability are before the court. Testamentary clauses that purport to exonerate a fiduciary from responsibility for failing to exercise prudence and reasonable care have been found invalid as contrary to public policy. While, historically, exoneration clauses have been a matter requiring judicial intervention, with the passage of § 11-1.7 of the N.Y. Estates, Powers & Trusts Law (EPTL) in 1966 testamentary attempts to immunize a fiduciary from liability have been eliminated by legislative fiat. Nevertheless, because EPTL 11-1.7 is limited by its terms to testamentary documents, judicial oversight in this area continues, and has become most apparent in recent years, in the context of *inter vivos* instruments.

This article examines the competing interests involved in the construction of a will or trust, provides a general background on exoneration clauses, and advocates for the amendment of EPTL 11-1.7 to limit the enforceability of exoneration clauses in *inter vivos* trust instruments and powers of attorney.

Principles of Construction and the Role of Public Policy

New York law authorizes an individual having testamentary capacity to dispose of property "in any manner and for any . . . purpose," provided that the disposition does not offend public policy.[1] Consistent with that principle, intent generally trumps all other concerns in construing testamentary instruments.[2] Courts are charged with effectuating that purpose by implementing each testator's testamentary scheme, determining the decedent's intentions from the plain language of the entire will, and construing the words memorialized therein in accordance with their ordinary meanings.[3]

Once ascertained, the testator's intent typically controls.[4] Although the testator's voice has been silenced by death, courts are duty-bound to effectuate his or her expressed testamentary wishes, regardless of any conflicts among clamoring litigants.[5] Neither the courts nor the beneficiaries of an estate have the power to substitute their own wants and desires for those of the decedent[6] – that is, unless the testator's intent violates public policy.[7]

A legacy is violative of public policy when it contravenes a constitutional provision, statutory prohibition, or "the social judgment . . . implemented by the statute."[8] When a testator's intent offends public policy, a court will circumvent it and substitute its discretion for that of the decedent.[9]

Examples of testamentary provisions that violate the law or public policy abound.[10] In *In re Walker*, the petitioners commenced a construction proceeding, seeking to obtain two adoption decrees they claimed the decedent, their adoptive father, specifically bequeathed to them in his will.[11] The petitioners sought the decrees because the documents purportedly identified their biological mothers.[12]

The Surrogate's Court, New York County, denied the petitioners' application and dismissed the petition, reasoning that public policy required the confidentiality of adoption records.[13] In affirming the surrogate's decision, the Appellate Division, First Department and the Court of Appeals relied upon the same policy-based rationale.[14] As the Court of Appeals explained, the decedent's bequest was "contrary to public policy because consummation of the transfer [was] sought for the purpose of discovering information which [was] against the public policy . . . to disclose without good cause."[15] The confidentiality was necessary to ensure the assimilation of the adopted child into the adoptive family and the privacy of the biological parents, among other concerns.[16]

Another case often cited for this proposition is *In re Haight*,[17] in which the decedent's will conditioned his son's right to enjoy the income of a testamentary trust on the son's divorce or separation from his wife. Although the Surrogate's Court, Orange County,

issued a decree effectuating that provision, the Appellate Division, Second Department, found it to be void as against public policy.[18] The Appellate Division reasoned that "conditions annexed to a gift, the *tendency* of which is to induce the husband and wife to live separate, or *to be divorced*, are, upon grounds of public policy and public morals, void."[19]

In re Pace[20] is of equal import. In *Pace*, the decedent's will directed the trustees of a testamentary trust to raze the buildings located on real property held in trust.[21] Noting that the buildings were in "good physical condition," the trustee commenced a construction proceeding and the Surrogate's Court, Cayuga County, found that the subject provision was void as against public policy.[22] The court explained that the decedent's intent should not be effectuated because razing the buildings would be "waste[ful]."[23] As the court further opined, "the intention of the maker of a will should not be carried out when the results would be absurd, abhorrent or a waste of the assets of an estate."[24] Accordingly, the court refused to enforce the disputed provision.[25]

In sum, while a testator's expressed intent generally guides the construction of a will, adherence to that intent is not universal. Courts can look beyond testamentary intent and substitute their discretion for that of a testator when the testator's intent violates the law or public policy of the state.

Exoneration Clauses: Meaning and Early Application

Estate and trust fiduciaries owe a duty of undivided, absolute loyalty to the beneficiaries whose interests they protect.[26] This "inflexible" duty of fidelity is akin to the highest standards of honor, not just honesty alone.[27] It obligates fiduciaries to administer the estate or trust for the benefit of the beneficiaries, without regard to self-interests.[28] The legal responsibilities arising from that fiduciary status cannot generally be divested by agreement or otherwise.[29]

Notwithstanding that duty, however, testators and grantors have attempted to insulate their fiduciaries from liability for breaching their obligations.[30] These attempts come in the form of exoneration clauses, which purport to exculpate fiduciaries for breaching the duty of undivided loyalty and failing to account.[31] Yet, these clauses are not universally enforceable, despite the intentions of testators, grantors and principals.[32]

More than a century ago, in *Crabb v. Young*, the Court of Appeals first addressed the issue of whether exoneration clauses are enforceable.[33] In *Crabb*, the decedent's will exempted the trustees of a testamentary trust established pursuant thereto from liability for "any loss or damage . . . except [that which occurred due to] their own willful default, misconduct or neglect."[34] When the trust suffered investment losses, the beneficiaries sought to be

reimbursed by the trustee.[35] Although both the trial court and intermediate appellate court ruled that the trustee had an obligation to replace the amount lost, the Court of Appeals reversed, relying on the exoneration clause contained in the will.[36] In doing so, the Court explained that the decedent "had an absolute right to select the agencies by which his bounty should be distributed and to impose the terms and conditions under which it should be done."[37] Since there was no evidence of willful default, misconduct or negligence on the trustee's part, the exoneration clause governed and required that the fiduciary be excused from liability for the losses.[38]

Subject to the requirement that fiduciaries act honestly and in good faith, the rule in *Crabb* prevailed for more than five decades, until the Legislature enacted N.Y. Decedent Estate Law § 125 (DEL) in 1936.[39] Section 125 of the DEL proscribed the enforcement of exoneration clauses that purported to excuse estate and testamentary trust fiduciaries from liability for failing to exercise reasonable care.[40] This was necessitated by the "increasing practice of testamentary draftsmen and corporate fiduciaries in vesting in . . . fiduciaries almost unlimited powers, with a minimum of obligations."[41] As the legislative history reflects, this practice was "a serious potential menace not only to the rights of a surviving spouse but of . . . all persons interested in estates."[42] The same policy-based reasons governed when the Legislature passed the successor to DEL § 125, EPTL 11-1.7, 30 years later.[43]

Whittling Away the Power to Exonerate Fiduciaries

Under EPTL 11-1.7, a testator is prohibited from exculpating the executor or testamentary trustee nominated in a will from liability for failing to "exercise reasonable care, diligence and prudence."[44] Will provisions that purport to do so are void as against public policy and have no effect.[45] Indeed, as Surrogate Radigan explained in *In re Stralem*, "'the attempted exoneration of the fiduciary [of an estate or testamentary trust] for any loss, unless occasioned by "willful neglect or misconduct" is a nugatory provision amounting to nothing more than a waste of good white paper.'"[46]

Countless cases bear this point out.[47] Surrogate Holzman's decision in *In re Lubin*[48] provides a helpful analysis of the statute as it relates to executors and testamentary trustees. In *Lubin*, the decedent's will provided that the executor of his estate would be relieved from liability "for any loss or injury to the property . . . except . . . as may result from fraud, misconduct or gross negligence."[49] Describing it as a "toothless tiger," the surrogate refused to enforce the exoneration clause because it violated public policy.[50]

Another noteworthy case is *In re Allister*, in which the decedent's will authorized her testamentary trustee to invest the trust principal "irrespective of whether the same may be authorized by the laws of [this] State . . . as investments for fiduciaries and without the duty to diversify and without any restrictions placed upon fiduciaries by any present or future applicable law."[51] Notwithstanding the testator's intent, however, the Surrogate's Court, Nassau County, found that the exoneration provision contravened EPTL 11-1.7,[52] reasoning that the provision "would elevate the fiduciary above the law" if effectuated.[53]

Although EPTL 11-1.7 undeniably applies to testamentary instruments, the statute is silent with respect to *inter vivos* trust instruments and powers of attorney.[54] That silence has left courts to reach their own, sometimes divergent, views on the issue and necessitates the amendments discussed below.

The Statutory Silence

As noted above, EPTL 11-1.7 is devoid of any mention of *inter vivos* trust instruments and powers of attorney.[55] In the absence of statutory guidance, courts have exercised their discretion – and reached conflicting conclusions – as to the enforceability of exoneration clauses in such instruments.

Initially, the Appellate Divisions for the First and Second Departments enforced exoneration clauses in *inter vivos* trust instruments,[56] relying upon the strong preference for respecting a grantor's expressed intent, rather than imposing judicial discretion on the trust.[57] The courts also emphasized that the exoneration clauses were limited – they did not completely absolve the fiduciaries from accountability to the trust beneficiaries.[58]

More recently, courts have come to contrary conclusions, holding that exoneration clauses in *inter vivos* trust instruments are not enforceable, despite the statutory silence in EPTL 11-1.7.[59] For example, in *In re Shore*, the Surrogate's Court, New York County, invalidated an exoneration clause that purported to insulate the attorney-trustee from the duty to account.[60] Accountability is the cornerstone of all fiduciary relations, said the court; the exoneration clause in question violated public policy since it left the trust beneficiary with no one to protect his interests.[61] The court explained that the "public policy against exonerating testamentary fiduciaries from any and all accountability is equally applicable [to] inter vivos trusts."[62] Accordingly, the court rejected the attorney-trustee's defense that the exoneration clause excused her from the duty to account.[63]

Similarly, in *In re Francis*, the only reported decision to address the enforceability of such clauses in powers of attorney, the Surrogate's Court, Westchester County, rejected the agent's reliance on an exculpatory provision that authorized him to engage in self-dealing and absolved him of the duty to account.[64] As Surrogate Anthony A. Scarpino, Jr. explained, the agent's conduct was governed by the "standard of 'utmost good faith and undivided loyalty toward the principal, [as well as] the highest principles of morality, fidelity, loyalty and fair dealing."[65] Insofar as the exoneration clause purported to excuse the agent from that standard, it ran "afoul of New York's public policy" and could not be enforced.[66]

Since executors, trustees, and agents acting pursuant to powers of attorney are held to the same standard of absolute, undivided loyalty to the beneficiaries whom they serve, public policy necessitates that they be treated similarly, especially in the context of exoneration clauses. Therefore, EPTL 11-1.7 should be amended to effectuate that purpose by filling the statutory void with respect to *inter vivos* trust instruments and powers of attorney, regardless of the grantor's or principal's expressed intentions. Indeed, doing so will ensure that the state's public policy concerns regarding reasonable fiduciary conduct are served and that the courts address this issue uniformly.

Conclusion

The language of testamentary and non-testamentary instruments, while generally accorded great deference by the courts, has historically yielded to public policy concerns – ensuring that a fiduciary acts in accordance with the highest principles of morality, fidelity, loyalty and fair dealing. Though traditionally invoked in the area of estates, these principles should apply equally in the context of every instrument from which a fiduciary relationship arises. Hence, there is no logical basis for excluding *inter vivos* trusts and powers of attorney from the scope of exceptions that have been applied to exoneration clauses. Indeed, giving *inter vivos* trustees and attorneys-in-fact unfettered discretion to act unreasonably, without accountability, contravenes the very nature of their fiduciary status. Section 11-1.7 should, therefore, be amended to ensure the interests of *inter vivos* trust beneficiaries and principals are protected by proscribing the enforcement of broad exoneration clauses, which purport to relieve fiduciaries from the duty to exercise reasonable care, diligence and prudence. ■

1. *In re Walker*, 64 N.Y.2d 354, 357–60, 486 N.Y.S.2d 899 (1985).

2. *Sankel v. Spector*, 8 Misc. 3d 670, 679–80, 799 N.Y.S.2d 356 (Sup. Ct., N.Y. Co. 2005); *see In re Fabbri*, 2 N.Y.2d 236, 239–40, 159 N.Y.S.2d 184 (1957).

3. *Walker*, 64 N.Y.2d at 358–60.

4. *Id.* at 358.

5. 11 Warren's Heaton on Surrogate's Court Prac. § 187.01(4)(a) (7th ed. 2007).

6. *Id.*

7. *In re Godrey's Will*, 36 N.Y.S.2d 414, 415 (Sur. Ct., Richmond Co. 1941).

8. *Walker*, 64 N.Y.2d at 358–60.

9. Warren's Heaton, *supra* note 5, at §187.01(4)(e).

10. *In re Liberman*, 279 N.Y. 458, 464–66, 18 N.E.2d 658 (1939) (holding a condition in restraint of marriage to be void as against public policy); *Kalish v. Kalish*, 166 N.Y. 368, 372–73, 59 N.E. 917 (1901) (opining that the testamentary provisions, which violated the rule against perpetuities, contravened the public policy of this state); *Levenson v. Levenson*, 229 A.D. 402, 403–406, 242 N.Y.S. 165 (2d Dep't 1930) (stating that the decedent's attempt to convey an interest in a joint tenancy was invalid); *In re McHugh*, 226 A.D. 153, 154, 234 N.Y.S. 541 (4th Dep't 1929) (invalidating a bequest of wrongful death action proceedings, which did not provide for the statutory beneficiaries); *Hacker v. Hacker*, 153 A.D. 270, 271–77, 138 N.Y.S. 194 (2d Dep't 1912) (finding a testamentary provision containing an unlawful restraint on the power of alienation to be invalid).

11. *Walker*, 64 N.Y.2d at 358–60.

12. *Id.*

13. *In re Walker*, 99 A.D.2d 448, 448–49, 471 N.Y.S.2d 243 (1st Dep't 1984), *aff'd*, 64 N.Y.2d 354, 358–60, 486 N.Y.S.2d 899 (1985).

14. *Id.*

15. *Walker*, 64 N.Y.2d at 360.

16. *Id.* at 360–61.

17. 51 A.D. 310, 311–12, 64 N.Y.S. 1029 (2d Dep't 1900).

18. *Id.* at 313–16.

19. *Id.*

20. 93 Misc. 2d 969, 400 N.Y.S.2d 488 (Sur. Ct., Cayuga Co. 1977).

21. *Id.* at 970–75.

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.*

26. 41 N.Y. Jur. 2d Decedents' Estates § 1450 (2009); Ian W. MacLean, *Exculpatory Clauses in* Inter Vivos *Trusts: What Remains of a Trustee's Duty of Undivided Loyalty?*, 37 NYSBA Trusts & Estates L. Section Newsl. 5, 5 (Fall 2004).

27. *In re Wallens*, 9 N.Y.3d 117, 122–23, 847 N.Y.S.2d 156 (2007) (discussing the duty of trustees).

28. *Id.*

29. *Id.*

30. MacLean, *supra* note 26, at 5.

31. Robert Whitman, *Exoneration Clauses in Wills and Trust Instruments*, 4 Hofstra Prop. L.J. 123, 124–25 (1992).

32. *Cf. In re Stralem*, 181 Misc. 2d 715, 720, 695 N.Y.S.2d 274 (Sur. Ct., Nassau Co. 1999) (discussing the enforcement of exoneration clauses in testamentary instruments).

33. 92 N.Y. 56, 65–67 (1883).

34. *Id.*

35. *Id.*

36. *Id.*

37. *Id.*

38. *Id.*

39. *In re Clark's Will*, 257 N.Y. 132, 138, 177 N.E. 397 (1931); *In re Balfe's Will*, 245 A.D. 22, 24–25, 280 N.Y.S. 128 (2d Dep't 1935); Margaret Valentine Turano, Commentaries: EPTL § 11-1.7 (2008).

40. *In re Stralem*, 181 Misc. 2d 715, 719–20, 695 N.Y.S.2d 274 (Sur. Ct., Nassau Co. 1999).

41. *Id.*

42. *Id.*

43. *Id.*

44. EPTL 11-1.7(a)(1).

45. EPTL 11-1.7(a)–(b).

46. *In re Stralem*, 181 Misc. 2d at 720 (citations omitted).

47. *See, e.g.*, *In re Allister*, 144 Misc. 2d 994, 998, 545 N.Y.S.2d 483 (Sur. Ct., Nassau Co. 1989); *In re Lang*, 60 Misc. 2d 232, 234–35, 302 N.Y.S.2d 954 (Sur. Ct., Erie Co. 1969).

48. 143 Misc. 2d 121, 539 N.Y.S.2d 695 (Sur. Ct., Bronx Co. 1989).

49. *Id.* at 122.

50. *Id.*

51. *Allister*, 144 Misc. 2d at 997–98.

52. *Id.*

53. *Id.*

54. *In re Shore*, 19 Misc. 3d 663, 665–67, 854 N.Y.S.2d 293 (Sur. Ct., N.Y. Co. 2008); *In re Francis*, 19 Misc. 3d 536, 541–43, 853 N.Y.S.2d 245 (Sur. Ct., Westchester Co. 2008).

55. Coincidentally, the Legislature recently amended the N.Y. General Obligations Law (GOL) to ensure greater accountability among agents acting pursuant to powers of attorney. GOL §§ 5-1505, 5-1509, 5-1510. Among other things, the amended GOL sections specify that agents owe fiduciary duties to their principals, provide for the appointment of monitors with respect to the agents, and authorize the commencement of special proceedings to remove agents. *Id.* The new provisions are consistent with the amendments to EPTL 11-1.7 proposed herein in that they provide for greater accountability among agents.

56. *Carey v. Cunningham*, 191 A.D.2d 336, 336, 595 N.Y.S.2d 185 (1st Dep't 1993); *Bauer v. Bauernschmidt*, 187 A.D.2d 477, 478–79, 589 N.Y.S.2d 582 (2d Dep't 1992); *see also Kolentus v. AVCO Corp.*, 798 F.2d 949, 966 (7th Cir. 1986) (applying New York law).

57. *Bauer*, 187 A.D.2d at 478–79.

58. *Carey*, 191 A.D.2d at 336.

59. *In re Amaducci*, N.Y.L.J., Jan. 12, 1998, p. 32, col. 3 (Sur. Ct., Westchester Co.).

60. *Shore*, 19 Misc. 3d at 665–67.

61. *Id.*

62. *Id.*

63. *Id.*

64. *In re Francis*, 19 Misc. 3d 536, 541–42, 853 N.Y.S.2d 245 (Sur. Ct., Westchester Co. 2008).

65. *Id.*

66. *Id.*