

**The Changing Rules of Attorney-Client Privilege in
Trust and Estate Matters**
or
Can a Trustee Only Confess to a Priest?

Bryn Mawr Trust Breakfast Seminar
September 13, 2017

J. Stoddard Hayes, Jr., P. Kristen Bennett, and Kari Springer
Gawthrop Greenwood, PC

Table of Contents

- I. INTRODUCTION
 - A. Background to the Fiduciary Exception
 - 1. The Exception Defined
 - 2. Origination
 - 3. Modern View
 - a. What privileges are involved?
 - b. How do they normally work?
 - c. What is the problem?
- II. PENNSYLVANIA AND THE FIDUCIARY EXCEPTION
 - A. Case Law in Pennsylvania
 - 1. *Pew Trust*
 - 2. *Follansbee v. Gerlach*
 - 3. *Thouron Estate (No. 2)*
- III. DELAWARE AND THE FIDUCIARY EXCEPTION
 - A. *Riggs National Bank of Washington DC v. Zimmer*
 - B. *Mennen v. Wilmington Trust Company*
 - C. New Delaware Law
- IV. EXAMPLE UNDER PENNSYLVANIA LAW
- V. EXAMPLE UNDER DELAWARE LAW
- VI. PRESENTER BIOGRAPHIES

I. INTRODUCTION

American courts have struggled with the question of whether a trustee may rely on the attorney-client privilege in order to prevent disclosure of communications between the trustee and counsel to the trust beneficiaries. There is still no clear or consistent answer to this question.

Pennsylvania and Delaware have both considered the issue and have applied the fiduciary exception differently.

In Pennsylvania, the exception was developed through case law and allows the beneficiary access to communications regarding administration of a trust, but not communications derived from anticipation or threat of litigation against the trustee. The Pennsylvania fiduciary exception does not always neatly apply and is a source of confusion in regards to the attorney-client privilege.

However, Delaware has adopted a statute providing that a fiduciary does not waive the attorney-client privilege in regards to administrative matters, but instead applies a three-part test to determine which party is the “real client.” Delaware has attempted to use legislation in order to make the fiduciary exception apply in a more straightforward manner.

A. Background to the Fiduciary Exception

1. The Exception Defined: A fiduciary cannot withhold communications with an attorney from the beneficiary when those services were related to administration of the trust *and* those services were paid for with assets of the fiduciary entity. The beneficiary is treated as a true client or joint client with the fiduciary of the attorney and therefore, the attorney-client privilege is not recognized. However, the attorney-client privilege still exists when the fiduciary seeks legal advice or information in anticipation or threat of litigation.
2. Origination: The fiduciary exception to the attorney-client privilege first originated in 19th century English trust cases. The English courts concluded communications between a fiduciary and his attorney must be disclosed to trust beneficiaries. *See In re Mason*, 22 Ch. D. 609 (1883); *Talbot v. Marshfield*, 2 Dr. & Sm. 549, 62 Eng. Rep. 165 (1865); *Wynne v. Humberston*, 27 Beav. 165, 54 Eng. Re. 165 (1858). These cases ultimately hold that because communications between a fiduciary and an attorney benefit the beneficiary, the communications must be disclosed to the beneficiary.

3. Modern View: Recent cases essentially follow the same reasoning as the early 19th century cases and reach the same holding, except an exception has been carved out in regards to whether the legal advice obtained was in anticipation of litigation or administration of the trust, the latter requiring disclosure to the beneficiary. Not until 1976, was the fiduciary exception imported into American law, in the case, *Riggs Nat'l Bank of Washington, D.C. v. Zimmer*, 355 A.2d 709 (Del. Ch. 1976).

a. What privileges are involved?

- i. The attorney-client privilege protects the confidentiality of communications between the client and attorney and is recognized as one of the oldest common law privileges for confidential communications.
- ii. There are exceptions to the attorney-client privilege. Some jurisdictions have established a fiduciary exception to the attorney-client privilege, which allows beneficiaries to access otherwise privileged communications between the fiduciary and the fiduciary's attorney. This exception may extend to work product created by an attorney for the administration of the trust as well.

b. How do they normally work?

- i. Generally, the attorney-client privilege applies to (1) a communication, (2) between lawyer and client, (3) in confidence, (4) for the purpose of obtaining or providing legal assistance for the client. Restatement 3rd of the Law Governing Lawyers.
- ii. The privilege encourages full communication between lawyers and their clients because it protects them from the risk that what they tell their lawyer will be involuntarily disclosed.

c. What is the problem?

- i. There are several problems in recognizing a fiduciary exception to the attorney-client privilege, namely, which party is the real client; does the source of funds to pay the legal fee matter; does a fiduciary have any protection from litigation by the beneficiary; and what types of documents must or should be produced to the beneficiary. These issues have muddied the waters in application of the fiduciary exception and Pennsylvania and Delaware deal with this issue differently.

- ii. In response to these problems, the Court of Common Pleas in Pennsylvania has recognized the fiduciary exception notably in the case of *Follansbee v. Gerlach*, 56 Pa. D. & C.4th 483 (Ct. Comm. Pl. 2002). The holding in *Follansbee* has also been upheld by other Pennsylvania courts, however, an appellate level Pennsylvania court has not yet heard a case on the fiduciary exception to the attorney-client privilege. In Delaware, the landmark case, *Riggs Nat'l Bank of Washington, D.C. v. Zimmer*, along with a statute carve out the fiduciary exception to the attorney-client privilege.

II. PENNSYLVANIA AND THE FIDUCIARY EXCEPTION

Pennsylvania has essentially thrown out the attorney work-product doctrine in matters brought against a fiduciary by a beneficiary. There are two main theories in regards to allowing beneficiaries access to privileged information:

1. Beneficiaries pay for the legal services through the trust so they should be able to see the communications.
2. Counsel for the fiduciary owes a derivative fiduciary obligation to the beneficiaries, therefore, anything counsel says to the fiduciary is not protected by the attorney-client privilege.

The law in Pennsylvania regarding the fiduciary exception has developed through case law. In Pennsylvania, a beneficiary of a trust is not a client of the trustee's attorney unless the parties have expressly come to such an agreement. Pennsylvania cases reason that a beneficiary should receive access to communications regarding trust administration because the trustee is obligated to provide such information and therefore, there is no attorney-client privilege in regards to matters of administration.

Since the exception in Pennsylvania largely developed through case law, the law is best understood in the context of the facts in those cases.

First, *Pew Trust* involved an action filed by the beneficiaries of a trust against the trust's former counsel for breach of fiduciary duties. The beneficiaries attempted to sue the former counsel for bad advice they received in regards to a transaction involving the trust.

In *Follansbee*, the beneficiaries filed an action against the former counsel of the trust and subpoenaed a third party for documents regarding the former counsel's management of the trust. The trustee opposed the subpoena on the grounds that the information was protected by the attorney-client privilege.

Finally, in *Thouron Estate* (2), the beneficiaries objected to an accounting of the deceased's estate and filed an action against the executor to produce documents related to the administration of an estate. The executor objected to producing the documents, believing that the information was protected by the attorney-client privilege.

A. Case Law in Pennsylvania:

1. *Pew Trust*: In Pennsylvania, a trustee's attorney represents only the trustee, not the trust beneficiaries. *Pew* held that "in the absence of an express agreement to the contrary, the only client of counsel to the fiduciary is the fiduciary." *In re Pew trust*, 16 Fiduc. Rep.2d 73 (O.C. Montgomery 1995).
2. *Follansbee v. Gerlach*: This case upheld the proposition that only the trustee's attorney represents the fiduciary, rejecting authority in other jurisdictions illustrating that trust beneficiaries are "true clients" of the attorney. 56 Pa. D. & C.4th 319, 483 (Civ Div. Allegh. 2002).
 - a. In *Follansbee*, the beneficiaries of a trust attempted to obtain documents from a bank. *Id.* The bank refused on the grounds that the documents were protected by the attorney-client privilege. *Id.* The document contained communications regarding administration of the trust. *Id.*
 - b. The Court acknowledged that most jurisdictions distinguish communications about potential liability from communications about trust administration, and apply the attorney-client privilege only to the former. *Id.* In reaching this result, some jurisdictions characterize the beneficiaries as the "true client" of the attorney. *Id.* Other jurisdictions have determined that the law places an obligation on the trustee to provide the beneficiaries with complete information regarding administration of the trust. *Id.* The Court in *Follansbee* determined the latter to be persuasive, rather than characterizing the beneficiaries as a true client of the attorney. *Id.*
 - c. The Court further reasoned that the "right of the beneficiaries to the trust-related documents flows from the trustee's fiduciary obligations, not from any attorney-client relationship." *Id.* at 489. This line of reasoning is in alignment with the landmark case regarding the fiduciary exception, *Riggs Nat'l Bank of Washington, DC v. Zimmer*. *Id* at 489-90.

3. *Thouron Estate* (No. 2): More recently, in *Thouron*, the Court acknowledged and agreed with *Follansbee* regarding a fiduciary's obligations to disclose information regarding trust administration to beneficiaries, but not information relating to "defensive interests of the trustee." 3 Fid. Rep.3d 443 (O.C. Chester 2013).

III. DELAWARE AND THE FIDUCIARY EXCEPTION

A. *Riggs National Bank of Washington DC v. Zimmer.*

1. Delaware Courts recognized the fiduciary exception in 1976 in *Riggs Nat'l Bank of Washington, DC v. Zimmer*, 355 A.2d 709 (Del. Ch. 1976). In *Riggs*, the Court of Chancery compelled the production of a legal memorandum prepared by the trustee's attorney over the trustee's objections based on communications between the trustee and his attorney and was not prepared in contemplated of litigation. 355 A.2d at 712-13. The trust paid the attorneys' fees related to the preparation of the memo. *Id.* The Court found that the attorney's legal services were for the benefit of the trust beneficiaries and that the trustee's fiduciary duty to the beneficiary required that the memo be produced. *Id.*
2. The Delaware court determined that the beneficiary was a "real client" based on three factors; (1) there was no pending or threatened litigation when legal advice was sought, (2) there was no purpose for the memorandum other than to benefit the trust, and (3) the attorney was paid out of the trust assets. The court determined that payment from trust assets is not determinative, but it does offer a strong indication of which party is the "real client."
3. In applying the three-part test, the Court in *Riggs* held that, the attorney-client privilege did not apply because the memorandum was obtained for the benefit of the beneficiaries and was not prepared in anticipation of litigation.

B. *Mennen v. Wilmington Trust Company.*

1. In *Mennen v. Wilmington Trust Company*, the beneficiaries alleged that the trustees violated their fiduciary duties and sought to compel the production of documents withheld by the trustee. 2013 WL 4083852. Wilmington Trust argued that *Riggs* was superseded by changes in Delaware law. Delaware adopted Rule 502(d) that identified six exceptions to the attorney-client privilege. *Id.* A fiduciary exception is not identified in the statute and Wilmington Trust argued that no exception existed because it is not in the statute delineating exceptions to the

attorney-client privilege. However, the Court decided *Riggs* is still good law in Delaware.

2. The court in *Mennen* also found no validity in the idea that a fiduciary exception does not exist because it is not listed in Rule 502(d) of the rules of evidence. Instead, *Mennen* looked to Rule 502 and Rule 501 of the Delaware Uniform Rules of Evidence and decided that *Riggs* remained illustrative of Delaware law regarding the attorney-client privilege. *Id.*
3. *Mennen* reasoned that *Riggs* turned on a determination of “who the real or ultimate client was, meaning the person for whose benefit the legal advice was procured.” *Id.* In applying the three-part test from *Riggs*, threat of litigation, purpose of communication, and payment source, the Court in *Mennen* held that the attorney-client privilege applied to documents procured for the benefit and protection of Wilmington Trust from the threat of litigation, but did not apply to documents relating to the power and duties in the Trust Agreement. *Id.* Therefore, documents in regards to general trust information and administration were required to be produced.

C. New Delaware Law

1. Delaware adopted a statute in order to help clear confusion regarding whether the attorney-client privilege applies to a fiduciary or if it falls under the exception, allowing the information to be disclosed to the beneficiary. 12 Del C. § 3333(a) provides that in a matter where the fiduciary pays from his or her own funds, all communications are within the attorney-client privilege. Under section 3333(b), unless the governing document indicates otherwise, when a fiduciary pays counsel fees from the trust, the fiduciary does not waive the attorney-client privilege, even if those communications “had the effect of guiding the fiduciary in the performance of fiduciary duties.”
2. This language appears to be contrary to Pennsylvania law, in which there is no attorney-client privilege for communications regarding administrative matters of the trust. However, the court in *Mennen* determined that *Riggs* is still good law, but the beneficiary carries the burden of proving that the three-part test applies to documents they seek to compel. *Mennen v. Wilmington Trust*, 2013 WL 4083852. Therefore, the new Delaware statute provides that a fiduciary does not waive the attorney-client privilege and looking to *Riggs*, the privilege applies unless the three-part test is met.

IV. EXAMPLE UNDER PENNSYLVANIA LAW

In Pennsylvania, if a beneficiary seeks to compel the production of certain documents related to the management or administration of the trust, a court would likely determine that since the communication was created for the purposes of trust administration, the fiduciary exception applies. In this instance, the documents would need to be produced to the beneficiary because it is outside of the attorney-client privilege.

V. EXAMPLE UNDER DELAWARE LAW

However, under the same scenario in Delaware, the fiduciary does not automatically waive the attorney-client privilege. Under a reading of the statute and analysis of *Riggs*, the fiduciary exception would apply and the fiduciary would be required to produce the documents only if the beneficiary was unable to prove that the communication was not due to pending or threatened litigation, there was no purpose other than to benefit the trust and therefore the beneficiary, and whether the trust paid for the legal advice is a factor that will be considered as well.

VI. PRESENTER BIOGRAPHIES

J. Stoddard ("Tod") Hayes, Jr., Esquire is a member of Gawthrop Greenwood, PC's Estates and Trusts Department. Tod practices in the areas of estate planning, business succession planning, trust and estate administration, personal and fiduciary income taxation, and non-profit corporation law. He may be reached at 610.696.8225 or jhayes@gawthrop.com.

P. Kristen Bennett, Esquire also is a member of the Estates and Trusts Department at Gawthrop Greenwood, PC. Kristen focuses her practice on estate planning and administration and trust administration, and she provides counsel on taxation and tax planning for businesses. She may be reached at 302.777.5353 or kbennett@gawthrop.com.

Kari Springer is a third-year law student at Villanova Law School and Law Clerk at Gawthrop Greenwood, PC. Kari received her undergraduate degree from the University of Notre Dame and majored in American Studies.