



# Litigating Self-Interested Fiduciary Transactions

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# Introduction

- Frequently in fiduciary litigation parties challenge self-interested transactions.
- Examples of self-interested transactions.
- In Texas, there is a presumption that these types of transactions are unfair and voidable.
- The burden is on the fiduciary to prove the fairness of the transaction.
- There are many procedural and substantive issues involved in litigating a self-interested transaction.

# Introduction

- This presentation will address:
  - The duty of loyalty,
  - Self-interested transactions,
  - Presumption of unfairness,
  - Gifts
  - Summary judgment issues, and
  - Trial issues.

# Duty of Loyalty



# Duty of Loyalty

- A fiduciary duty is a formal, technical relationship of confidence and trust imposing higher duties upon the fiduciary as a matter of law.
- The duty owed is one of loyalty and good faith, strict integrity, and fair and honest dealing.
- When parties enter a fiduciary relationship, the fiduciary consents to have its conduct toward the other measured by high standards of loyalty as exacted by courts of equity.

# Duty of Loyalty

- To uphold its duty of loyalty, a trustee must meet a sole interest standard and handle trust property solely for the benefit of the beneficiaries.
- Other fiduciaries (RIAs) may owe a best interest standard of loyalty.
- There is a difference between the two, but both are exacting standards.

# Duty of Loyalty

- As part of a duty of loyalty, a fiduciary should generally only benefit from the relationship by being fairly compensated where allowed.
- Reasonable compensation is an exception to the sole-interest duty of loyalty.
- Texas statutes discuss compensation of fiduciaries, i.e., trustees, executors, POA agents, guardians, etc.

# Duty of Loyalty

- Other than reasonable compensation, other benefits are generally prohibited.
- Examples include kickbacks, investments of fiduciary property in agent's businesses, loans of fiduciary property to agent, agent's loans (with interest) to principal, etc.
- There are statutory exceptions when self-interested transactions are allowed.
- Further, agents are allowed to hire themselves in other capacities, i.e., legal work.

# Self-Interested Transactions



# Self-Interested Transactions

- A self-interested transaction is a transaction where the fiduciary could benefit in its individual capacity.
- The presumption includes transactions involving the fiduciary and a third party, conducted on behalf of the beneficiary of the fiduciary relationship.
- “Texas courts have applied a presumption of unfairness to transactions between a fiduciary and a party to whom he owes a duty of disclosure, thus casting upon the profiting fiduciary the burden of showing the fairness of the transactions.”

# Self-Interested Transactions

- To establish the fairness of a transaction between a fiduciary and his principal, relevant factors include:
  - (1) there was full disclosure regarding the transaction,
  - (2) the consideration (if any) was adequate,
  - (3) the beneficiary had the benefit of independent advice,
  - (4) the party owing the fiduciary duty benefited at the expense of the beneficiary, and
  - (5) the fiduciary significantly benefited from the transaction as viewed in light of the circumstances in existence at the time of the transaction.

# Self-Interested Transactions

- As the first factor to prove fairness, full disclosure is also a very important aspect of proving the fairness of self-interested transactions.
- For example, in *Jordan v. Lyles*, heirs challenged a POA's transferring a significant portion of the principal's property into JTROS accounts. 455 S.W.3d 785 (Tex. App—Tyler 2015, no pet.). The jury found for the heirs, but the trial court awarded the agent a judgment notwithstanding the verdict.
- The agent was unable to prove that she specifically discussed the transactions with the principal and informed him of the material facts relating to them.
- Because the agent failed to show that she had fully disclosed the transactions, there was evidence that she breached her fiduciary duty. The court of appeals reversed and reinstated the jury verdict.

# Presumption of Unfairness



PRESUMPTION

# Presumption of Unfairness

- Put in context, the presumption in fairness only applies to the breach element of a breach of fiduciary duty claim.
- A plaintiff has the burden to prove:
  - a fiduciary relationship exists,
  - a self-interested transaction occurred, and
  - the amount of damages/benefits.

# Presumption of Unfairness

- What is a presumption and what does it do?
- There are many presumptions in the law that allow a party to prove one fact and presume another.
- A presumption shifts the burden of production from the party relying upon it to the other party regarding the presumed fact.
- A court has defined a presumption as a rule of law “by which the finding of a basic fact gives rise to the existence of the presumed fact, until the presumption is rebutted.”

# Presumption of Unfairness

- There are two types of presumptions: conclusive and rebuttable.
- A conclusive presumption cannot be rebutted, and once it is established, the opposing party cannot offer evidence to contradict it.
- A rebuttable presumption, however, can be rebutted by evidence; and where there is evidence to the contrary, the presumption simply disappears, and a factfinder cannot weigh it or treat it as evidence.

# Presumption of Unfairness

- Where the party opposing the presumption fails to produce any contrary evidence, the presumption is established conclusively.
- A party attempting to use a presumption must prove the underlying facts for the presumption with direct evidence.
- Where the party opposing the presumption produces contrary evidence and the presumption disappears, the evidence that originally gave rise to the presumption still retains whatever independent evidentiary value that it has and may be considered by the factfinder in determining the issue.

# Presumption of Unfairness

- The main reason for a presumption is its impact on the burden of proof.
- The burden of proof has two separate components.
- First, the burden of proof means the burden of persuasion, i.e., the burden to persuade the trier of fact that evidence supports a proposition.

# Presumption of Unfairness

- The burden of persuasion generally stays on the same party throughout the trial and never shifts.
- Secondly, the burden of proof means the burden of production, i.e., the burden to go forward and produce sufficient evidence in order to meet a prima facie case.
- The burden of production can shift back and forth between the parties depending upon the evidence that is produced.

# Presumption of Unfairness

- Normally, one party will initially bear both the burden of persuasion and the burden of production, and where the burden of persuasion does not shift to the other party, the burden of production may shift back and forth as each side produces evidence.
- Once a presumption is established it only shifts the burden of production, and places the burden on the opposite party to produce evidence to the contrary.
- It generally does not, however, shift the burden of persuasion to the other side.

# Presumption of Unfairness

- There is authority, however, that regarding the presumption of unfairness for fiduciary self-interested transactions, that both the burden of persuasion and production shift to the fiduciary.
- The Texas Pattern Jury Charge states: “In fiduciary duty cases, however, the presumption of unfairness operates to shift both the burden of producing evidence and the burden of persuasion to the fiduciary.”
- According to this authority the presumption of unfairness is a super presumption that shifts both the burden of production and persuasion to the fiduciary.
- But it is still a rebuttable presumption, and a fiduciary can produce evidence to rebut the presumption though it will continue to have the burden of persuasion to prove the fairness.

# Presumption of Unfairness

- Difference between a regular presumption and the super presumption.
- There is authority that the presumption of unfairness is not a super presumption; but just a normal presumption.
- This precedent primarily arises in the context of a will contest where a POA agent obtains a better will.
- *In re Estate of Klutts*, No. 02-18-00356-CV, 2019 Tex. App. LEXIS 11063 (Tex. App.—Fort Worth December 19, 2019, settled by agr.).
- So, Texas currently has authority that the presumption of unfairness is a super presumption and some authority that it is just a regular presumption.

# Gifts



# Gifts

- A common issue involving self-interested transactions is gifts from a principal to the fiduciary.
- For example, it is common for a parent to name a child as his or her power of attorney and then later want to give a gift to the child/agent. Is that gift presumptively unfair and void?
- Ordinarily, transfers from the principal to the fiduciary without adequate consideration are considered unfair transactions that are void.

# Gifts

- However, though the fiduciary has the burden to prove the fairness, he or she can do so by showing that the principal wanted to make a gift and had mental capacity to do so.
- “[W]e find it worth repeating that fiduciary status does not prohibit the beneficiary from giving the fiduciary gifts or bequests; instead it insures that the fiduciary will be prepared to prove the transaction was conducted with scrupulous fairness.”
- One way to establish decisively that a transaction was fair to the principal is to show that the principal consented to it.
- Texas courts have recognized the significance of the principal’s consent in determining whether a transaction by a profiting agent was fair or constituted self-dealing.

# Summary Judgment Standards



# Summary Judgment

- Traditional motion: Texas Supreme Court held in 1980s that a movant in a traditional summary judgment proceeding could not rely upon a presumption to shift the burden of production to the opposing party.
- However, courts are not consistent in applying this rule.
- Nonmovant can rely on a presumption to raise a fact issue.

# Summary Judgment

- A no-evidence summary judgment movant cannot file such a motion on a claim or defense on which it has the burden of proof.
- Normally, a breach of fiduciary duty plaintiff has the burden of proof on his or her claim and cannot file a no-evidence motion on that claim.
- However, in a self-interested transaction situation, the defendant/fiduciary has the burden to prove the fairness of the transaction, that he or she did not breach a fiduciary duty.
- A movant usually has to submit evidence to create a prima facie case for a presumption
- Once that is established, there is a presumption of unfairness that the trustee has a burden of production to prove was fair.
- If a plaintiff cannot attach any evidence to a no-evidence motion, how can it ever set up the presumption?.

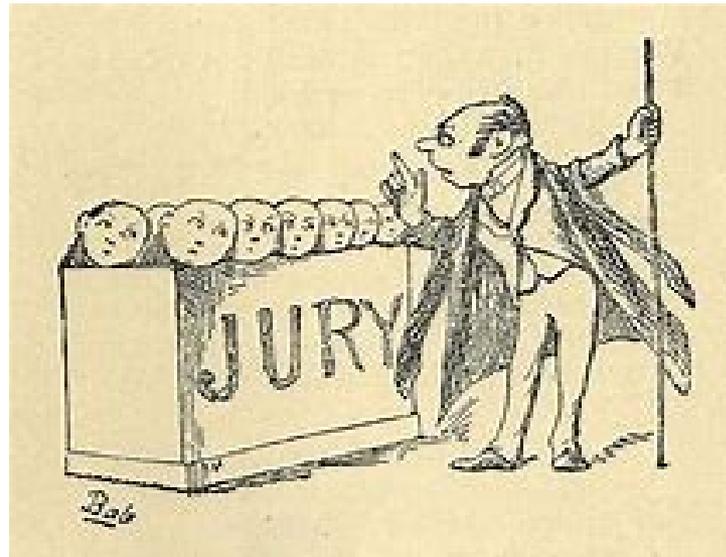
# Summary Judgment

- Undoubtedly, some courts will hold that they cannot review evidence to set up a no-evidence ground, and will deny the motion outright.
- But, some courts would allow a court to review evidence attached to the no-evidence motion.
- This would allow a plaintiff to attach evidence to a no-evidence motion to set up the fact that a self-interested transaction occurred, and then the no-evidence burden would initially be on the defendant to create an issue of fact on the fairness of the transaction.
- Also, potential use of a dual motion.

# Summary Judgment

- A fiduciary in a self-interested transaction case should not be able to file a no-evidence because it would have the burden of proof to establish the fairness of the transaction and a no-evidence movant cannot file such a motion on a claim or defense that it has the burden of proof to establish.
- There are very complex procedural issues when presumptions are used in summary judgment proceedings.

# Trial Issues



# Trial Issues

- Right to open and close.
- Dead Man's Rule
- Sufficiency of the evidence: legal sufficiency and factual sufficiency
- Directed Verdict
- Charge: objections to sufficiency and correct allocation of burden of proof.
- Motion for JNOV/Motion for New Trial

# Conclusion



# Conclusion

- Due to the strong duty of loyalty that fiduciaries owe their principals, there is a presumption of unfairness that attaches to any self-interested transaction.
- This presumption impacts all phases of a case and creates very complex procedural issues.
- The author hopes that this paper is helpful to practitioners and courts when faced with these thorny issues.