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The "Great Wealth Transfer" and Litigation Against Trustees

Fifteen years ago, John and Julie Jones,[1] both of whom were in their mid-60s, created a revocable trust to which they contributed all of the assets comprising their considerable wealth. As is often the case, the trust instrument named John and Julie as the initial co-trustees; in the event both John and Julie became unable to serve, a longtime family friend and colleague, Bill Brown, was designated as first alternate successor trustee, and the Jones' oldest son Jimmy was second alternate successor. At the death of the second trustor to pass away, Jimmy and siblings are to receive generous — seven-figure — distributions, but the bulk of the estate is to go to a local charitable foundation.

During their trusteeship, John and Julie have caused significant charitable distributions to be made from the trust — sometimes, but not always, honoring Jimmy's requests for contributions to *his* preferred charities. In addition, there have been sporadic gifts to Jimmy and his siblings.

A few months ago, John was found incompetent to manage trust affairs; shortly thereafter, when the same determination was made as to Julie, Bill Brown accepted his appointment as successor trustee.

Jimmy quickly expressed his dissatisfaction with Brown's management of the trust and his belief that he, rather than Brown, should be the trustee, and Jimmy made it known that he has retained counsel for that purpose. Brown feels strongly that by serving as trustee, he is properly carrying out the wishes of John and Julie.

What can Brown anticipate from Jimmy? And what should Brown be doing to prepare for litigation or to ameliorate the risk of suit being filed?

The Impending "Great Wealth Transfer"

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Type “Great Wealth Transfer” into a search engine, and you’ll quickly be looking at a long list of articles describing the impending transfer of trillions of dollars in assets from baby boomers to heirs and others. You’ll find estimates ranging from $30 trillion to $120 trillion. Pick either number or something in between; the further reality is that a hefty portion of those assets are held in the estates of high-net-worth individuals. By one estimate, nearly one-third of that soon-to-be-transferred wealth is held by the top 1% of households.

One would reasonably expect (and experience confirms) that many of those high-net-worth individuals, with access to skilled attorneys and advisors, will have chosen to place their wealth into trusts for ultimate disposition instead of planning for its passage by will. During the lifetimes of the trustors who commonly serve as the initial trustees, a natural reticence for familial conflict will tend to inhibit public discord over the validity or administration of the trust. But when a triggering event occurs — the trustors’ deaths or, as in the hypothetical above, their incapacity — and the trustee no longer is a family member, that reluctance typically subsides, and the potential for litigation increases correspondingly.

Potential Allegations Against the Trustee

So, in our hypothetical situation, regardless of the merit (or lack thereof) of Jimmy’s allegations, what might Brown anticipate from a court filing in Jimmy’s quest for ownership of, or control over, trust assets?

One potential contestant strategy is an attack on validity of the trust instrument itself, if the consequence of setting it aside would be intestacy with Jimmy benefitting as a statutory heir. As with a will contest, the claim might be that the settlors, John and Julie, lacked mental capacity to execute the document; or they were subjected to undue influence in doing so; or both.

Perhaps more common is a suit to remove and replace the trustee. Under the Uniform Trust Code — some variation of which has been adopted in 36 states — a court may remove the trustee at the behest of the settlor, a cotrustee, or a beneficiary (or *sua sponte*) under the following conditions:

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- The trustee has committed a serious breach of trust;
- Lack of cooperation among cotrustees substantially impairs the administration of the trust;
- Because of unfitness, unwillingness, or persistent failure of the trustee to administer the trust effectively, the court determines that removal of the trustee best serves the interests of the beneficiaries; or
- There has been a substantial change of circumstances or removal is requested by all the qualified beneficiaries, the court finds that removal of the trustee best serves the interests of all the beneficiaries and is not inconsistent with a material purpose of the trust, and a suitable cotrustee or successor trustee is available.[2]

The court may also retain equity jurisdiction for actions against a trustee, such as for breach of fiduciary duty, independent of statutory grounds.[3]

An action to remove the trustee often also includes a claim for surcharge — seeking a money judgment against the trustee for disgorgement of fees paid to the trustee or reimbursement of other disbursements from the trust. The apparent rationale is that a trustee faced with a threat of personal liability, however remote it may appear, might choose to resign rather than defending his or her trusteeship in litigation.

Protective Action by the Trustee

So, what should the trustee do to head off, or prepare to defend, litigation in which an unhappy heir or other potential beneficiary seeks his or her removal? While no approach guarantees immunity from litigation, the measures below may alleviate the litigation risk.

Review the trust instrument(s) for exculpatory language.

In most jurisdictions, settlors have broad authority to include exculpatory language that reduces or eliminates a trustee's exposure for ordinary negligence or less culpable conduct in trust administration.[4] Thus, trust instruments commonly limit trustee

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liability to wilful misconduct or bad faith. Statutes and case law vary from state to state, but generally the trust instrument cannot shield a trustee from liability for breaches of trust amounting to intentional misconduct, gross negligence, or reckless indifference, or for profit obtained through breach of trust. But a trustee should not be forced to defend his or her trusteeship against claims arising out of mistakes or errors in judgment in good faith administration of the trust.

It would of course be prudent for a *potential* trustee to conduct such a review in advance of, and even as a condition of, allowing him or her to be named as trustee or successor trustee — at a point in time when revision of the trust instrument is possible. In the more common situation, where the trustee's administration is being evaluated in light of a threatened or asserted claim, the instrument will hopefully contain exculpatory language that will support a dispositive motion if litigation commences.

Create and preserve evidence of the settlors' capacity and intent.

If it is anticipated that the potential attack may include claims of undue influence and/or lack of capacity, and if the settlors are still alive and competent, the trustee should consider recording video interviews in which the settlors reaffirm their intent as to, and the reasons underlying, the distribution plan set out in the documents they executed.

Seek counsel; ensure compliance with ongoing obligations under the trust instrument and applicable statutes.

Statutes commonly require a trustee to provide notice to beneficiaries upon the occurrence of a triggering event,[5] to keep beneficiaries reasonably informed concerning trust administration, [6] and to provide specified information to beneficiaries on request. [7] The trust instrument may impose additional notice obligations or, within limits, reduce the statutory requirements. A trustee should seek and follow counsel's protective advice concerning the scope of the trustee's duties and limitations on his or her authority.

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Obviously, the record will have closed as to acts or omissions predating the threat or filing of litigation, but the trustee and his or her counsel should take pains to avoid unforced errors in ongoing administration as litigation ensues or continues.

Communicate frequently — through counsel, if appropriate — with heirs and other interested parties.

As mentioned above, probate statutes typically will (and the trust instrument may) set out requirements for notices to be given to beneficiaries and heirs. Over and above those requirements, frequent communications with those individuals (or their counsel) concerning developments in trust administration may avoid or at least ameliorate claims of trustee inattention or hostility.

Focus the court's attention on the contestant's "hidden agenda."

The grounds on which a disgruntled heir or beneficiary might seek the removal of the trustee have been thoroughly plowed; the claims and causes of action that one would expect in a petition for removal or surcharge are familiar. Often the facts pled by the contestant reflect nothing more than disappointment with the settlors' estate plan or disagreement with the trustee's good faith decisions — and don't readily fit into the legal theories pled by the contestant. In that situation, the trustee and his or her counsel should focus the arguments, in motion practice or at trial, on the mismatch between the facts on the ground and the theories supposedly supporting removal. The hidden agenda may be personal enrichment, or societal standing accompanying the trustee's ability to direct charitable contributions, or some other motive, but it never hurts to give your court reason to feel good about ruling in favor of the trustee.

Key Takeaway

In our experience, an individual typically agrees to serve as trustee out of loyalty to and respect for high-net-worth friends, along with a desire to preserve and enhance their legacies. Unfortunately, acceptance of responsibility for the administration of the trust often comes accompanied by the need to defend litigation brought

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by unhappy heirs and beneficiaries. If you find yourself in that situation, you have our best wishes — and our availability to provide counsel to help you defend and carry out the settlors' intentions for the administration and disposition of a lifetime's accumulated wealth. Should you need further guidance or assistance, reach out to the author or any member of our Wealth Planning & Family Office team.

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[1] The named characters are fictitious, and the scenario, though realistic, is hypothetical.

[2]Uniform Trust Code § 706. *See also, e.g.,* Cal. Prob. Code § 15642 (b)(2), (4) (additional statutory grounds include "…the trustee is insolvent or otherwise unfit to administer the trust … [or] fails or declines to act …").

[3] *See, e.g., People ex rel. Becerra v. Shine,* 259 Cal. Rptr. 3d 700 (Cal. App. 2020) (trial court found that trustee violated fiduciary duties by, e.g., loaning trust funds to friends).

[4] *See, e.g.,* Cal. Prob. Code § 16461.

[5] *See, e.g., id.* §16061.7 (notice within 60 days of a revocable trust becoming irrevocable due to the death of one or more settlors or a change of trustee of a revocable trust).

[6] *See, e.g., id.* §16060.

[7] *See, e.g., id.* §16061.

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