Article

Too Much for Too Little: The Restatement's Measure of Damages Where the Trustee Sells a Trust Asset for an Insufficient Price

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The *Restatement (Third) of Trusts: Prudent Investor Rule* contains a standard for measuring damages from the authorized but negligent sale of trust property that, especially when real estate is involved, could yield damages incongruently large compared with the duty to which the beneficiaries are entitled. This Article argues that, when a trustee negligently sells trust property for too little, the correct measure of damages should place the beneficiaries in the position they would have occupied had the trustee met his duty of care—not some other position they would have occupied had the trustee more than met that duty.

In particular, this Article argues that, when a trustee sells a trust asset for an insufficient price, the measure of damages stated in *Restatement (Third)* section 205 cmt. d[1]—that the beneficiaries should be awarded the difference between the actual sale price and the value of the asset at the time of sale—is based on the wrong standard.[2] The standard of care incorpo-

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1. RESTATEMENT (THIRD) OF TRUSTS: PRUDENT INVESTOR RULE § 205 cmt. d (1992) (including comment d by reference in the Appendix). References in the article to "*Restatement (Third)*" refer to the *Restatement (Third) of Trusts: Prudent Investor Rule* and not the recently revised *Restatement (Third) of Trusts*. *See infra* note 2.

2. The *Restatement (Third) of Trusts* was revised and newly adopted as of May 18, 2011. In the revision, section 205 has been revised and renumbered as *Restatement (Third) of Trusts* section 100. RESTATEMENT (THIRD) OF TRUSTS § 100 (2011). Though the revisions include changes to some language and elimination of the specific language in comment d, the revised language

rated in comment d is not one merely of reasonableness, but of perfection. The rule should be that beneficiaries are awarded the difference between the actual sale price and the lowest price at which a comparable but reasonable trustee could have sold the asset. In this way, damages are based on the standard of care owed by the trustee, not a higher standard.

Restatement (Third) section 205(b) provides the applicable general rule, "A trustee who commits a breach of trust is . . . chargeable with the amount required to restore the values of the trust estate and trust distributions to what they would have been if the trust had been properly administered."[3]

Calculating the amount prescribed by section 205(b) is not always easy. Because there generally are more ways than one to administer a trust properly, and because those different ways can result in different values, there is not necessarily only one number that represents the combined values of "what [the values of the trust estate and trust distributions] would have been if the trust had been properly administered."[4] In actuality, those values can differ greatly. Where the values differ significantly, how should a court choose among them in calculating damages under section 205(b)? Comment a to section 205 suggests that the court take an ad hoc approach, comparing the performance of the trust as breached to the performance of the same or any other trust the court reasonably might choose.[5] But the *Restatement* leaves unanswered the question of which comparable performance the court should choose, and why.

Four examples illustrate the apparent attraction of an ad hoc approach. In all four examples, the trustees have power to sell the properties out of the trust.

First, consider a case where Trustee A sells Blackacre for $299,000 based on a negligently performed (or obtained) appraisal. The purchaser soon thereafter resells Blackacre for

results in the same conclusions as those reached in this article, and referencing the *Restatement (Third) Trusts: Prudent Investor Rule* and comment d provide for a clearer and more succinct analysis of the issues presented by the Prudent Investor Rule.

3. RESTATEMENT (THIRD) OF TRUSTS: PRUDENT INVESTOR RULE § 205(b).

4. *See id.*

5. *Id.* § 205 cmt. a ("In most cases appropriate return rates might be based on total return experience (positive or negative) for other investments of the trust in question, or possibly that of portfolios of other trusts having comparable objectives and circumstances. . . . In some cases, especially involving breaches of short duration, it may be appropriate simply to charge the trustee with interest rather than looking to total return.").

$600,000. At trial, the court finds that there was no material change in the market between the first and second sales, and that the $600,000 price upon resale was the fair market value of Blackacre at the time of Trustee A's sale. The Court awards damages of $301,000. Based upon comment d to section 205, this would seem to be the right result: "[i]f the trustee is authorized to sell trust property, but in breach of trust he sells it for less than he should receive, he is liable for the value of the property at the time of the sale less the amount which he received."[6]

Second, assume two identical properties, Blackacre and Whiteacre. Trustee A sells Blackacre out of the Blackacre Trust for $299,000. Trustee B sells Whiteacre out of the Whiteacre Trust for $300,000. The beneficiaries sue, alleging that each sale was for too little. For convenience, the trials are consolidated. The evidence demonstrates, and the judge finds, that a trustee could reasonably have performed (or obtained and relied upon) appraisals anywhere between $300,000 and $700,000 at the time of sale. Thus, Trustee A is liable for negligence, but Trustee B is not. Weighing the competing reasonable appraisals, the judge finds that the actual value of each property at the time of sale was $600,000. Under comment d, the beneficiaries of the Blackacre Trust would be entitled to damages in the amount of the difference between the value of the property ($600,000) and the actual sale price ($299,000), or $301,000. But the beneficiaries of the Whiteacre Trust would be entitled to nothing, because their trustee was not liable to begin with, having sold Whiteacre for a price within the range of reasonable values.[7] Is it right that Trustee A is liable for $301,000 because he sold Blackacre for $1,000 less than a reasonable trustee could have? This second example suggests that

6. *Id.* § 205 cmt. d (including comment d by reference in the Appendix); *see also In re* Green Charitable Trust, 431 N.W.2d 492, 506 (Mich. Ct. App. 1988) ("[W]here liability is based on selling property for less than its fair value, the general rule is that the loss to the trust is measured by the difference between the fair value and the amount received, or the amount the estate would otherwise have received."); RESTATEMENT (SECOND) OF TRUSTS § 205 cmt. d (1957) (same); 4 AUSTIN W. SCOTT ET AL., SCOTT AND ASCHER ON TRUSTS § 24.9 (5th ed. 2007) ("When a trustee who is authorized to sell an item of trust property does so but in breach of trust sells it for less than its full value, the trustee is chargeable with the difference between the value of the property at the time of the sale and the amount received.").

7. *See* RESTATEMENT (THIRD) OF TRUSTS: PRUDENT INVESTOR RULE § 204; RESTATEMENT (THIRD) OF TRUSTS § 99 (2011); 4 SCOTT ET AL., *supra* note 6, § 24.8.

the correct measure of damages is not the difference between the property's actual value and its actual sale price, but the difference between the lowest price at which a reasonable trustee could have sold the property and its actual sale price.[8] By awarding $1000 in damages, the court places the beneficiaries in the position they would have occupied if Trustee A had obtained an appraisal that was not negligent. And that is the stated goal of § 205(b)—restoring the values of the trust estate and trust distributions to what they would have been if the trust had been properly administered.

The third example involves the same sale of Blackacre. Assume that Trustee A in the past has always obtained and relied on appraisals from Reasonable Appraisal Services. In selling Blackacre, however, he carelessly obtained and relied on an appraisal from Negligent Appraisal Services. At the resulting trial, Trustee A testifies he would have used Reasonable Appraisal Services if he had not breached his duties as trustee. Reasonable Appraisal Services, in turn, testifies that it would have appraised Blackacre at $500,000. In this instance, but for the breach, the trust estate would have received $500,000 rather than $299,000. If the goal of section 205(b) is to put the beneficiaries in the place they would have been if the breach had not occurred, it would seem that they should be awarded $201,000 rather than only $1000.[9]

Now take a fourth example. There are only six appraisers in town. Trustee A randomly but reasonably would have picked any of the five others if he had not negligently picked the one bad apple who appraised Blackacre at $299,000. Of the five appraisers who were not negligently involved, one testifies he would have appraised Blackacre at $700,000. The second and third both testify $600,000. The fourth testifies $300,000. The fifth testifies $500,000. Should the Court base its award on some sort of average?[10] Doing so seemingly would place the

8. The correct measure of damages will also include an appropriately determined amount to compensate for any loss suffered by the trust from the lack of use of the money lost in the negligent sale.

9. For the case on which this example is loosely based, see *In re* Estate of Janes, 630 N.Y.S.2d 472 (Sur. Ct. 1995), *aff'd as modified sub nom.*, *In re* Janes, 643 N.Y.S.2d 972 (App. Div. 1996), *aff'd sub nom.*, *In re* Estate of Janes, 681 N.E.2d 332 (N.Y. 1997).

10. *See* Leister v. Dovetail, Inc., 546 F.3d 875, 881 (7th Cir. 2008) ("But the valuation by Leister's expert witness of the benefits that the 401(k) account would have yielded was erroneous, though accepted by the district judge. It was based not on the average performance of the investment vehicles

beneficiaries in a position that might not be exactly the one they would have occupied had the breach not occurred, but at least would be closer to it.

That the four examples each emphasize a different factor that seems persuasive in choosing the "right" damages amount makes understandable the endorsement in section 205(b) of a discretionary, ad hoc approach to the calculation of damages when a trustee negligently sells trust property for too little. But such an approach is innately unsatisfactory because it allows arbitrariness and inequality of result.

The author believes there is one correct result for all four examples. Oddly, it most clearly is not the result prescribed by comment d, the difference between fair market value and actual sales price. By measuring damages as the difference between the actual value of the property at the time of sale and the amount the trustee received, comment d creates an incongruity between the measure of a trustee's performance and the measure of his liability. Whereas a trustee's duty is merely to sell property for a price that is reasonable,[11] comment d measures damages on the assumption that, if the trustee had not been negligent, he would have sold for a price that was perfect; i.e., actual or market value.

Measuring damages based on the price the trustee would have obtained if he had followed his normal routine (example 3) falls prey to the same criticism. Unless the settlor's agreement with the trustee, or some other enforceable interest such as estoppel, establishes that the standard of care is to be defined as the trustee's personal standard of care, as opposed to the standard of care set forth in the Prudent Investor Rule,[12] measuring damages according to the trustee's own normal conduct awards the beneficiaries a different (presumably greater) amount than they are entitled to.

in which the contributions might have been placed but on the performance of the best of those vehicles, as improperly determined ex post.").

11. *See, e.g.*, Ansell v. First of Am. Bank–Mich., N.A. (*In re* Harold S. Ansell Family Trust), 569 N.W.2d 914, 916 (Mich. Ct. App. 1997) ("We agree with the probate court that, in the absence of bad faith, unfair dealings, or a conflict of interest, the adequacy of a price obtained by a trustee for a piece of the trust property should be reviewed for an abuse of discretion. . . . Furthermore, even if the land was more valuable than the price obtained by the trustee, we find that, considering the marketing limitations imposed on the trustee by petitioner, the trustee did not abuse its discretion in selling the land for $875,000."). *See generally* RESTATEMENT (THIRD) OF TRUSTS: PRUDENT INVESTOR RULE § 227 (1992).

12. *See supra* note 1 and accompanying text.

Finally, measuring damages according to the average performance of all reasonable trustees would hold negligent trustees to the standard of the average reasonable trustee. But that is too high a standard. The correct standard is the performance of any reasonable trustee.

Absent the establishment of a right otherwise, beneficiaries have a right to expect that their trustee will perform at the level of a reasonable trustee. They have no right (as opposed to mere optimism) to expect that their trustee will perform at some higher level, such as that of a perfect trustee, an average reasonable trustee, or the particular trustee's own normal behavior. Damages should compensate the beneficiaries for the right of which they were deprived, not for some greater right they never had. Where a trustee negligently sells trust property for an insufficient price, the measure of damages should be the difference between the lowest price at which a reasonable trustee could have sold the property and its actual sale price, plus an appropriately determined amount to compensate for any loss suffered by the trust from the lack of use of the money lost in the negligent sale.