NOT FOR PUBLICATION WITHOUT THE
APPROVAL OF THE APPELLATE DIVISION

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
DOCKET NO. A-4056-14T2

IN THE MATTER OF THE MAY 1,
1992 MARK FAMILY TRUST

and

IN THE MATTER OF THE DECEMBER 29,
1992 MARK FAMILY TRUST.

Argued June 8, 2016 – Decided August 5, 2016

Before Judges Fuentes, Koblitz and Gilson.

On appeal from Superior Court of New Jersey, Chancery Division, Monmouth County, Docket Nos. P-386-13 and P-388-13.

Eric H. Lubin, argued the cause for appellants Ann Mark, Eric Benjamin Mark, Felicia Rochelle Mark Damato and Jacqueline Eva Mark Goldschneider (Lomurro, Munson, Comer, Brown and Schottland, LLC, attorneys; Mr. Lubin, on the brief).

Jared J. Scharf, respondent, argued the cause pro se.

PER CURIAM

Petitioners Ann Mark and her three children, Eric Benjamin Mark, Felicia Rochelle Mark Damato and Jacqueline Eva Mark Goldschneider appeal from an April 17, 2015 order granting summary judgment to respondent Jared Scharf, the former trustee of the Mark family trusts and denying summary judgment to

petitioners. Petitioners sought removal of respondent as trustee and reimbursement for losses incurred by his investment in a hedge fund controlled by his son.[1] Because the trust instruments do not immunize respondent from a violation of his fiduciary duties, we reverse the order granting summary judgment in favor of respondent and grant partial summary judgment on liability in favor of petitioners.

In 1992 petitioner Ann Mark created two irrevocable trusts for the benefit of her three children, one in May and one in December. Respondent became the successor trustee for both trusts in 1997. Eleven years later, respondent took some of the assets from the May 1992 Trust and formed three separate trusts, each one naming an individual child as the sole beneficiary. Each trust's instrument states that it is governed by the laws of New York.

In April 2010 respondent invested a total of $450,000 from the three individual trusts in a hedge fund named BGS Economies of Scale LLC (BGS). Respondent's son Adam[2] and two others started the hedge fund. Adam is an attorney with no formal training or license related to trading securities. Prior to the

[1] The parties informed us respondent is no longer the trustee, but the issue of reimbursement remains.

[2] We refer to respondent's son by his first name for clarity and intend no disrespect.

investment of the trusts' funds in BGS, the hedge fund had made no trades. The trusts were the only outside investor. Respondent agreed to pay Adam's hedge fund an annual 2% management fee based on the total value of the investment, as well as 20% of all profits generated.

By the end of 2010, the hedge fund had generated a return of 14.35%. On February 9, 2011, respondent informed petitioners he intended to increase the total investment in BGS and, for the first time in writing, advised them that his son was a principal in BGS. Ultimately, the total investment in BGS rose to $2,200,000. BGS then suffered a 14.16% loss in 2011, decreasing the three individual trusts' combined investment by $336,010. At the end of 2011, two of the founding partners of BGS left the hedge fund with their investments, leaving Adam as the sole owner of a new company, JOS Advantage LLC (JOS), which managed the trusts' hedge fund investments as well as those of Adam's extended family.

After the two principals left, JOS suffered substantial losses. From January 2012 until the end of November 2014, the trusts' investments with JOS suffered combined losses totaling approximately $869,702. At the beginning of 2015 respondent withdrew the trusts' funds from JOS. From April 2010, when respondent initially invested the trusts' funds in BGS, to

December 2014, the overall value of the trusts increased significantly from $30,260,499 to $36,127,538.

Beginning in May 2013 petitioners sought the immediate withdrawal of the trusts' funds from JOS, but respondent refused these requests. Later in 2013 petitioners filed a complaint against respondent seeking his removal as trustee and reimbursement for losses incurred by his imprudent investments. On January 2, 2015, nearly twenty months after the petitioners first asked that the trusts' funds be removed from JOS, Adam transferred the funds.

After oral argument on the cross-motions for summary judgment, the motion judge issued a decision from the bench granting respondent's motion for summary judgment:

> I find that the trust agreement reigns this case, that the trust agreement allowed the trustee to do exactly what he did. To hold and retain all property received from any source without regard to diversification, risk, productivity or the trustee's personal interest in such property in any other capacity. It also allowed him to employ persons even if they were associated with the trustee, to advise or assist the trustee in the performance of the trustee's duty.
>
> . . . .
>
> . . . . the plaintiffs arguing well that this small thing that he did was a breach of fiduciary duty, . . . the Court finds it was not . . . and the trustee was not unsuitable in making that decision.

Although the trust instruments are governed by the laws of New York, "the procedural law of the forum state applies even when a different state's substantive law must govern." N. Bergen Rex Transp., Inc. v. Trailer Leasing Co., 158 N.J. 561, 569 (1999). We apply the same standard as the motion judge in assessing a motion for summary judgment. Townsend v. Pierre, 221 N.J. 36, 59 (2015).

"A trial court shall grant summary judgment if 'the pleadings, depositions, answers to interrogatories and admissions on file, together with affidavits, if any, show that there is no genuine issue of material fact challenged and that the moving party is entitled to a judgment or order as a matter of law.'" Badiali v. N.J. Mfrs. Ins. Grp., 220 N.J. 544, 555 (2015) (quoting R. 4:46-2(c)). "At this stage of the proceedings, the competent evidential materials must be viewed in the light most favorable to . . . the non-moving party, and [he or] she is entitled to the benefit of all favorable inferences in support of [his or] her claim." Bagnana v. Wolfinger, 385 N.J. Super. 1, 8 (App. Div. 2006).

Pursuant to New York law, "it is elemental that a fiduciary owes a duty of undivided and undiluted loyalty to those whose interests the fiduciary is to protect." Birnbaum v. Birnbaum, 539 N.E.2d 574, 576 (N.Y. 1989). The duty "not only [bars]

blatant self-dealing, but also requir[es] avoidance of situations in which a fiduciary's personal interest possibly conflicts with the interest of those owed a fiduciary duty." Ibid. Included in the scope of the duty "is every situation in which a trustee chooses to deal with another in such close relation with the trustee that possible advantage to such other person might influence, consciously or unconsciously, the judgment of the trustee who is in duty bound to consider only the interest of his [or her] cestui que trust." Albright v. Jefferson Cty. Nat'l Bank, 53 N.E.2d 753, 756 (N.Y. 1944). The trustee's actions must be entirely for the benefit of the beneficiaries:

> when the trustee has a selfish interest which may be served, the law does not stop to inquire whether the trustee's action or failure to act has been unfairly influenced. It stops the inquiry when the relation is disclosed and sets aside the transaction or refuses to enforce it, and in a proper case, surcharges the trustee as for an unauthorized investment. It is only by rigid adherence to these principles that all temptation can be removed from one acting as a fiduciary to serve his [or her] own interest when in conflict with the obligations of his [or her] trust.
>
> [In re Estate of Rothko, 379 N.Y.S.2d 923, 943 (Sur. Ct. 1975), modified on other grounds, 392 N.Y.S.2d 870 (App. Div.), aff'd, 372 N.E.2d 291 (N.Y. 1977).]

The prohibition against self-dealing includes "transactions . . . with a spouse, agents, employees and other persons whose interest are closely identified with those of the trustee." Bogert, The Law on Trusts and Trustees § 543 (2d Ed. Rev. 1993 & Supp. 2013). Transactions involving a child, however, are not per se violations of the rule. In re Parisi, 975 N.Y.S.2d 459, 462 (App. Div. 2013) (holding that a sale of property by the trustee, husband of the decedent, to his son does not automatically have to be set aside pursuant to the "no further inquiry" rule). While the facts here do not evidence blatant self-dealing, respondent's investment in a hedge fund in which his son was first one of three partners and then the sole manager, constitutes a conflict of interest.

"As a fiduciary, a trustee bears the unwavering duty of complete loyalty to the beneficiaries of the trust no matter how broad the settlor's directions allow the trustee free rein to deal with the trust." Boles v. Lanham, 865 N.Y.S.2d 360, 361 (App. Div. 2008); see N.Y. Est. Powers & Trusts Law § 1-2.7 (Consol. 2016). New York law, however, also provides that "the rule of undivided loyalty due from a trustee may be relaxed by a settlor by appropriate language in the trust instrument in which he [or she], either expressly or by necessary implication, recognizes that the trustee may have interests potentially in

conflict with the trust." O'Hayer v. De St. Aubin, 293 N.Y.S.2d 147, 151 (App. Div. 1968) (citation omitted). "[T]he language limiting the general rule is strictly construed so that the trustee's actions will not be approved if he [or she] trespasses outside the boundaries of the powers granted." Ibid.

The motion judge mistakenly interpreted the language of Article VII paragraphs A, B, and L of each trust, which define the powers of the trustee, as containing exculpatory clauses that absolved respondent of his fiduciary duty of undivided loyalty to the beneficiaries. Paragraph A exculpates the trustee from inaction with regard to trust-owned property, giving the trustee the power:

> A. To hold and retain all or any property received from any source, without regard to diversification, risk, productivity, or the Trustee's personal interest in such property in any other capacity, and to keep all or part of the trust property at any place within the United States or abroad.
>
> [(Emphasis added).]

Conversely, paragraph B, covering investments, contains no such exculpatory language with regard to self-dealing when giving the trustee the power:

> B. To invest and reinvest the trust funds (or leave them temporarily uninvested), in any type of property and every kind of investment, including (but not limited to) corporate obligations of every kind, preferred or common stocks, securities of

> any regulated investment trust, and partnership interests.

The trust instrument protects the trustee when he or she has taken no action, but no such protection is afforded when the trustee invests the trust's property. Had the grantors intended to exculpate the trustee from his or her fiduciary duties when investing they would have explicitly provided for it, as evidenced by the exculpatory language included in paragraph A.

Paragraph L allows the trustee "[t]o employ persons, even if they are associated with the Trustee, to advise or assist the Trustee in the performance of the Trustee's duties." (Emphasis added). The motion judge's interpretation negates the distinction between investing and employing a person to assist the trustee. Respondent invested in his son's hedge fund. He did not employee Adam as a financial advisor. The agreement allowed the trustee to employ his son Adam. Investing in Adam's hedge fund, however, created a situation that divided respondent's loyalty between his son and the beneficiaries of the trusts, to whom he owed a fiduciary duty.

Applying the exculpatory provisions of paragraph A and L, which relate to the retention of trust assets and the employment of advisors, to the investment provision of paragraph B is inconsistent with the plain language of the agreement. Reading paragraph B narrowly, as we must under New York law, there is no

language exculpating respondent from the conflict of interest he engaged in when he invested the trusts' assets in his son Adam's hedge fund. See In re Jastrzebski, 948 N.Y.S.2d 689, 691 (App. Div. 2012) (noting that explicit language allowing a trustee to transact with entities in which he had an interest "in [his] sole and nonreviewable discretion" was sufficiently explicit exculpatory language to alter his duty of loyalty).

Because there is no language at all in the trusts' documents insulating respondent from liability for investing despite his conflict of interest, respondent breached his duty of undivided loyalty by investing in his son's hedge fund. Respondent's claim that his initial investment in BGS was motivated by Adam's partners' previous successes and investment experience does not mitigate the conflict of interest. Respondent does not dispute Adam benefitted financially from the fees he received from the trusts' investments. Respondent continued to invest in the hedge fund long after Adam's partners had left, despite the continued losses suffered by the trust investments. Nothing in this record demonstrates a ratification by the beneficiaries of the investment in Adam's hedge fund. Moreover, it is undisputed that the beneficiaries objected to the investment in Adam's fund beginning in 2013. Respondent has raised no material issues of fact regarding whether or not he

invested in his son's hedge fund. Respondent violated his fiduciary duty to the beneficiaries because this investment created a conflict of interest that resulted in a financial loss to the trusts.

Respondent minimized the investment in Adam's hedge fund, stating that "only a negligible portion of the trust's assets were at risk." This may be relevant to damages, but does not affect the conflict of interest. We reverse the order granting summary judgment in favor of respondent, and grant partial summary judgment on liability in favor of petitioners. No disputed material facts exist as to respondent's breach of his fiduciary duty. The remaining issue of damages is remanded for further proceedings.

Reversed and remanded. We do not retain jurisdiction.