IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

No. 27273

GLORIA LOOS, LOUIS HOHN,
EVELYN LANG, VIRGINIA BINDER,
AND GENE LOOS,

Appellants,

v.

ROBERT AND PAUL BORMANN,

Appellees.

Appeal from the Circuit Court
First Judicial Circuit
Hutchinson County, South Dakota

HONORABLE GLEN ENG
HONORABLE PATRICK SMITH

APPELLANTS' BRIEF

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Notice of Appeal filed November 26, 2014

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Preliminary Statement

References to the settled record as reflected by the Clerk's Index will be to the designation (R). References to the appendix will be to the designation (App.).

Statement of Jurisdiction

The Petitioners appeal from the circuit court's Order and Judgment allowing and approving Trustees' Annual Account and Dismissing Objections filed October 14, 2014 (R. 1012); Order on Renewed Motions for Summary Judgment filed July 16, 2014 (R. 952); Order on Motions for Summary Judgment filed April 30, 2014 (R. 875); Decree of Settlement of Annual Account and Report of Trustees filed February 4, 2013 (R. 588); Decree of Settlement of Annual Account and Report of Trustees filed January 24, 2012 (R. 575); Decree of Settlement of Annual Account and Report of Trustees filed January 25, 2011 (R. 562); Decree of Settlement of Annual Account and Report of Trustees filed January 26, 2010 (R. 549).

Notice of entry of each of these orders was served by U.S. mail by Appellee Trustees on October 29, 2014. (R. 1016.) The Petitioners served a timely notice of appeal dated November 26, 2014. (R. 1039 & 1057.) This Court has jurisdiction pursuant to SDCL § 15-26A-3(1), (2), or (4).

Request for Oral Argument

The Petitioners respectfully request the privilege of appearing for oral argument.

Statement of the Issues

1. Trustee Robert Bormann has a son who is married to a daughter of Lorin Schmidt. The Trustees leased 320 acres of the Trust's farm land to Schmidt at a lower rental rate than any other tenant received without disclosing the relationship or preferential rate to the beneficiaries or the circuit court. Does the lease constitute self-dealing under *In re Estate of Stevenson*, 2000 S.D. 24, 605 N.W.2d 818?

   The circuit court held as a matter of law that the relationship was not close enough to constitute self-dealing.

   - *Estate of Stevenson,* 2000 S.D. 2, 605 N.W.2d 818

2. In addition to the initial nondisclosure of the Schmidt relationship, the Trustees refused to promptly provide information that would have revealed the Schmidt relationship and preferential rate and, among other things, commingled records concerning other matters with Trust records, caused the Trust to incur late fees that they did not reimburse, omitted 240 of 920 acres of Trust property from multiple years of accountings, and obtained liability insurance for only 680 out of 920 acres of property. Do these acts and omissions constitute breaches of trust and, if so, does the cumulative effect of all their breaches constitute a serious breach of trust warranting the Trustees' removal?

   The circuit court held that the Schmidt transaction and nondisclosure were not breaches of trust and concluded that it did not have the power to remove the Trustees.

   - SDCL § 55-3-20.1
   - Uniform Trust Code § 706, comment on Subsection (b)(1)

3. The accountings provided to the beneficiaries and circuit court covering years 2009 to 2012 did not disclose, among other things, the Schmidt

relationship or preferential rate and did not list 240 of the Trust's 920 acres. Were there material omissions from the accountings that prevent the Trustees from claiming that they have no liability pursuant to SDCL § 21-22-30?

The circuit court held as a matter of law that there were no material omissions from the accountings and thus the Trustees were discharged from all liability for 2009 to 2012 accounting periods.

- SDCL § 21-22-30
- SDCL § 21-22-14
- SDCL §§ 21-22-22 to 23

4. The Petitioners moved for summary judgment on their claims, including voiding the Schmidt lease, removing the Trustees, and recovering damages for the preferential rate given to Schmidt. What remedy, if any, are the Petitioners entitled to for the Trustees' acts or omissions?

The circuit court held as a matter of law that the Schmidt relationship was not close enough to constitute self-dealing and that there were no material omissions, hence it found that the Trustees should not be removed, the Schmidt leases should not be voided, and the Trustees had no personal liability.

- *Estate of Stevenson,* 2000 S.D. 2, 605 N.W.2d 818
- *Willers v. Wettestad*, 510 N.W.2d 676, 680-81 (S.D. 1994)

Statement of the Case

This appeal involves a court supervised trust over which the circuit court exercised no meaningful supervision. The circuit court's lack of supervision allowed the trustees to continuously and seriously breach the trust to the detriment of the elderly current income beneficiaries. This appeal raises important issues concerning a trustee's duty to disclose conflicts concerning a trust transaction to elderly beneficiaries and to the supervising circuit court and concerning a trustee's

duty to administer a trust in a non-adversarial manner solely for the benefit of the beneficiaries.

On November 19, 2013, four of the five current income beneficiaries of Joseph Baumgart's testamentary trust (the "Trust") petitioned the supervising circuit court to remove the Trustees and replace them with an independent third-party trustee, to reopen accountings for years 2009 to 2012, to obtain copies of the leases of Trust property for years 2007 to 2013, and to award damages caused by the Trustees' breaches. (R. 595.) These claims were based on the Trustees' failure to provide copies of trust leases to beneficiaries upon request and Petitioners' discoveries that one Trustee, Robert Bormann, had leased Trust property to the father-in-law of Bormann's son and that the annual accountings had omitted this relationship, the identity of the individual tenants, the rent paid by the individual tenants, as well as failing to list 240 of the Trust's 920 acres. The Petitioners later learned that, for years, Robert Bormann's son's father-in-law rented Trust property at a substantially lower rate than any other tenant. The Petitioners and Trustees filed cross-motions for summary judgment. On April 30, 2014, Circuit Court Judge Glen Eng granted the Trustees' motion as to all accountings approved by the Court before January 1, 2010, based on SDCL § 21-22-27, but otherwise denied both parties' motions. (App. 001.)

Both parties renewed their motions for summary judgment. In addition, the Trustees petitioned to have their 2013 accounting approved, and the Petitioners objected. On July 16, 2014, the circuit court granted the Trustees' motion for summary judgment concerning the 2009-12 accountings, concluding that they contained no material omissions. (App. 003) It denied summary judgment as to removal of the Trustees. (*Id.*)

On September 12, 2014, the circuit court granted the Trustees' motion to dismiss Petitioners' objection to the 2013 account based on the Schmidt transaction. (App. 179, p. 15.) At the end of the hearing, the circuit court found that the Trustees had not committed any breaches of duty and denied the petition to remove the trustees. (App. 230-31 at p. 218, 221-22.) By order filed October 14, 2014, it accepted and approved the 2013 accounting. (App. 004.) On October 29, 2014, the Trustees served by mail the Notice of Entry of the circuit court's orders dated: October 14, 2014; July 16, 2014; April 24, 2014; February 4, 2013; January 24, 2012; January 25, 2011; and January 26, 2010. ®. 1016.) The Petitioners have appealed from all of these orders.

Statement of the Facts

The Joseph Baumgart Trust was created in 1980 and has been supervised by the Circuit Court in Hutchinson County since its creation. (App. 033 ¶ 26.) In 1992, Robert and Paul Bormann became co-trustees of the Trust. (App. 181, p.

23.) They are individual trustees, not corporate trustees. Other than a small cash reserve for expenses, the Trust consists of 920 acres of farm real estate located in Hutchinson and Douglas counties. (Ex. 113.)

The income beneficiaries at the time of the orders appealed from were: Gloria Loos, Louis Hohn, Evelyn Lang, Virginia Binder, and Lorraine Woodworth. Loos, Hohn, Lang, and Binder are the four Petitioners.[1] They range in age from 82 to 95 years old. (App. 219, p. 175-76.) The other beneficiary, Woodworth, lives in Washington state and has minimal contact with her Baumgart relatives. She is an invalid and has no living children. (App. 225, p. 197.)

According to the terms of the Trust, when the last income beneficiary dies, the land will be sold and sale proceeds will be paid to any children of the original beneficiaries living at that time. Gene Loos is the son of Gloria Loos, and thus is one of the contingent remainder beneficiaries. Gene is the attorney-in-fact for Gloria pursuant to a power of attorney. (Ex. 15, email dated Jan. 19, 2013.)

Each year, the Trustees must provide an accounting and obtain court approval of the accounting. The Bormanns' practice was to send the accounting and notice of hearing on the accounting to the current income beneficiaries. The accountings consisted of a short document giving the legal description of 620 acres of the Trust's real estate and the checking account balance at the end of the year.

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[1]Mr. Hohn passed away on October 6, 2014.

(App. 135-38.) A one-page exhibit was attached listing the total rental income for the year, along with the annual expenses. (*Id.*) The beneficiaries also received a notice of hearing providing a date when the accounting would be presented to the Court. The information provided to the beneficiaries did not, however, identify the tenants, the rent charged to the various tenants, or include copies of the leases with individual tenants. Nor did it inform the beneficiaries that any other information would be presented to the court. No notice of any of the proceedings, prior to the 2013 accounting, was sent to any of the remainder beneficiaries.

Until the hearing to approve the 2013 accounting, the Trust's attorney did not appear at the hearing in person. He mailed an order approving the accounting to the Court. (Ex. 11.) The cover letter stated that he did not expect the beneficiaries to appear. (*Id.*) The orders stated that the court had "fully examined the said account and report and the vouchers produced in support of the same." (App. 009.) The "vouchers" were envelopes containing miscellaneous documents concerning the Trust. (App. 194, p. 73.) The cover letter, order, and the vouchers were not served on the beneficiaries. (*Id.*) The vouchers typically did not include transaction documents, such as leases, and often were not filed until well after the date of the order stating that the circuit court had reviewed the voucher materials. The docket reveals that in 2010 the order approving accounting for 2009 was filed January 26, 2010, but the voucher was not filed until October 19, 2010; in 2011 the

order approving accounting for 2010 was filed January 25, 2011, but the voucher was not filed until May 9, 2011; in 2012 the order approving accounting for 2011 and vouchers were both filed on January 24, 2012; and in 2013 the order approving accounting for 2012 was filed February 4, 2013, but the voucher was not filed until November 13, 2013. Some of the Trust vouchers contain materials related to non-Trust matters handled by the Trustees. (App. 194-95, p. 76-79; Ex. 14.)

For many years, the Trust property was rented to members of the Bialas and Thuringer families. (App. 184, p. 33.) In August 1997, the Trustees terminated Jim Thuringer's lease. (Ex. 20; App. 200, p. 97-98.) That fall, one of Trustee Robert Bormann's sons married a daughter of a local farmer named Lorin Schmidt. (App. 199, p. 96.) Bormann's son and Schmidt's daughter had a child together a couple of years prior to the wedding. Unbeknownst to the beneficiaries, the Bormanns decided to rent the 320 acres previously rented to Thuringer to Lorin Schmidt. (App. 200, p. 98.) Before agreeing to lease the land to Lorin Schmidt, the Bormanns did not notify any other local farmers that Thuringer's land was available to rent. (*Id.*)

A review of the leases for years 2009-14 shows that the Bormanns charged Schmidt a lower per acre rental rate than any other tenant:

Crop Year	Lorin & Barbara Schmidt Douglas/Hutchinson 160 acres/160 acres	DuWayne/Travis Bialas Douglas 200 acres	Craig & Stacey Bialas Hutchinson 160 acres	Kurt/Willard Bialas Hutchinson 160 acres	Larry & Zita Bialas Hutchinson 80 acres
2009	$66.13/$72.25	$86.25	$86.25	$83.38	$82.31
2010	$66.13/$72.25	$86.25	$86.25	$83.38	$82.31
2011	$66.13/$72.25	$86.25	$86.25	$83.38	$82.31
2012	$80/$87.50	$105	$105	$105	$105
2013	$80/$87.50	$105	$105	$105	$105
2014	$135/$150	$165	$165	$165	$165

(App. 064-134.[2]) This table shows that the rent charged to Lorin Schmidt was always at least 10% lower than the rent charged to the Bialas tenants. If the comparison is limited to Douglas county land, the rent charged to Lorin Schmidt was over 20% lower.

The soil rating for each tenant's land is:

	Lorin & Barbara Schmidt Douglas/Hutchinson	DuWayne/Travis Bialas Douglas	Craig & Stacey Bialas Hutchinson	Kurt/Willard Bialas Hutchinson	Larry & Zita Bialas Hutchinson
Soil Rating	.796/.821	.837	.865 & .874	.853	.801

[2]The Trustees did not produce a clean copy the 2011 leases. It appears that the Trustees marked up their copy of the 2011 leases while preparing the 2012 leases, but the typed 2011 rental amount is still visible.

(Source: Pet. Ex. 17.) As this table shows, Lorin Schmidt's Hutchinson county land has a higher soil rating than the Hutchinson county land leased to Larry and Zita Bialas, yet the rent charged to Schmidt was always at least 10% lower. It also shows that the land leased to the four Bialas tenants had soil ratings ranging from .801 to .874, yet they were all charged the same uniform rental rate in 2012-14. From 2009-11, Willard was charged a lower rental rate than Travis, even though Willard's land has a higher soil rating.

The historical evidence concerning crop yields shows that, in some years, the Schmidt land produced better yields, whereas in others the Bialas land may be more productive. For example, in 1998, Schmidt's Douglas county land produced significantly more corn and almost as much soybeans as the Bialas land, but in 2005 the Bialas land in Douglas county had better results. (Ex. 7 & 8.) In 2005, Schmidt's Hutchinson county land produced significantly more corn than the three Bialas parcels in Hutchinson county, and produced significantly more soybeans than two out of the three Bialas parcels. (Ex. 7.) In his worksheet for the 2009 ACRE Program, Schmidt reported average direct yields for Hutchinson county of 54 for corn and 26 for soybeans, very close to the averages reported by Craig Bialas of 55 for corn and 28 for soybeans. (Ex. 6.)

During the hearing, Robert Bormann acknowledged that, in 1998, Schmidt's yields were "comparable" to the Bialas tenants, (App. 200, p. 99), and

that the numbers from the 2009 ACRE worksheets were "close." (App. at 102, p. 101-02.) He further acknowledged that, in 2005, Schmidt's Hutchinson county land generally outperformed the Bialas land, (App. 202, p. 105-06), and that yields in any given year can "vary wildly." (App. 202, p. 106.) Bormann admitted that the Trustees did not find out what the yields on the parcels have been for 2007-13, and thus do not know how Schmidt's yields have compared with the Bialas tenants since 2006. (App. 200-201, p. 100-01.) Bormann contended that he set the initial cash rental rates in 2007 based on the average yields for the time period 2003-06. (App. 201, p. 101.) Bormann's data, however, average all of the Bialas parcels in one lump sum, even though each Bialas parcel was separately leased.

Bormann's data shows that the average yield for Schmidt's Douglas county land from 2003-2006 was 72.38 for corn and 31.24 for soybeans, whereas the Bialas land in Douglas county averaged 113.12 for corn and 36.38 for soybeans. (Ex. 104.) When looking at the individual parcels, however, Schmidt's Douglas County bean average was actually higher than two of the Bialas parcels located in Hutchinson County. (App. 263, yield table.) The Schmidt and Bialas land in Hutchinson county were equally productive during this time period. Schmidt's Hutchinson county land averaged 94.37 for corn and 36.42 for soybeans, whereas the Bialas land averaged 96.88 for corn and 32.56 for soybeans. (*Id.*) Again, when looking at the individual parcels, Schmidt's Hutchinson County land

outperformed many of the individual Bialas parcels. (*Id.*) The data Bormann claims to have relied on from 2003-06 do not justify why Schmidt's rental rates have always been lower than the Bialas rates.

Because the accountings did not include the leases or information on individual tenants, the Trustees did not provide any disclosure to the beneficiaries concerning Robert Bormann's personal relationship with Lorin Schmidt. Nor did they disclose that Schmidt was being charged a lower rental rate than any of the Bialas tenants. Consequently, these facts went undiscovered for many years.

An additional reason these facts remained hidden is that the accountings for years 1993 through 2012 contained the legal description for only 680 acres of land. (App. 053-54 ¶ 3.) Accordingly, when Gene Loos, acting as Gloria Loos' attorney-in-fact, reviewed the accountings for 2009, 2010, and 2011, the information available to him concerning rental rates in the accounting was merely the total rent collected and the legal description for 680 acres. (App. 219, p. 173.) When Loos divided the total rent by 680 acres to estimate the rental rate, the omission of 240 acres made the per acre rental rate appear much higher than the Trust was actually receiving. (*Id.*) Loos therefore assumed the rents were near fair market levels. (*Id.*) In fall 2012, however, Louis Hohn–one of the other beneficiaries--told Loos at a family function that the Trust owned 900 acres. (App.

219, p. 175.) Loos responded that the accountings showed 675, but he would check when the next accounting was due and get back to Hohn. (*Id.*)

On January 7, 2013, Loos asked the Trust's attorney to provide the total number of acres owned by the Trust. (Ex. 15, email dated Jan. 7, 2013.) He repeated the request on January 10, 2013, and received a reply stating "approximately 900 acres." (*Id.*, emails dated January 10, 2013.) On January 19, 2013, Loos sent an email as the attorney-in-fact for his 90-year old mother Gloria, stating that, if the Trust owned 900 acres, the per acre rental rate for 2012 would have been approximately $100 acres, and even lower in previous years. (*Id.*, email dated Jan. 19, 2013.) Concerned that this appeared to be below market, Loos asked the Trust's attorney to provide the rental rates for each parcel of land from 2007-12 and an estimate of the 2013 rent. (*Id.*) Loos asked for a response before the hearing scheduled for February 4, 2013 to approve the 2012 accounting. (*Id.*) The Trust's attorney responded that he was checking with the Trustees and would get back to Loos. (*Id.*, Jan. 13, 2013 email.) The Trust's attorney did not provide a response, however, because he believed Robert Bormann had spoken to Loos. (App. 214, p. 154.)

Robert Bormann did call Loos before the February 4, 2013 hearing. (App. 220, p. 177.) Bormann explained that the 2013 rent had already been negotiated, and that the Trustees had not raised the rent because 2012 had been a bad drought

year. (App. 220, p. 178.) During the conversation, Bormann did not identify the individual tenants or provide any information on the rates charged to each tenant. (App. 220, p. 177-78.) As a result, at that time, no one provided Loos with the requested information concerning rental rates on individual parcels for 2007-12.

As the time for negotiating 2014 leases approached, Loos researched average rental rates for the area. The 2013 SDSU South Dakota Farm Real Estate Survey listed the average rental rates for nonirrigated cropland in Bon Homme, Hutchinson, and Yankton counties as $170.40, and in Charles Mix and Douglas counties as $125.00. (Ex. 16; App.221, p. 181-82.) These numbers were significantly higher than the $100 average rental rate that the Trust was receiving, so on August 28, 2013, Loos emailed Robert Bormann and requested that the Trustees meet with the beneficiaries to discuss what the 2014 rental rates should be. (Ex. 15, Aug. 28, 2013 email.) During conversations with Bormann, Loos renewed his attempts to obtain copies of past leases, but was not provided with any copies. (App. 221, p. 183.) During this process, however, Loos discovered Robert Bormann's personal relationship with Schmidt. (*Id.*)

Because the Trustees were being unresponsive, Loos engaged an attorney who sent a letter requesting that the Trustees resign and provide copies of past leases. (Ex. 15, Sept. 9, 2013 letter.) In exchange for their resignation, the beneficiaries offered to waive any claims against the Trustees and release them

from any liability. (Ex. 15, Sept. 9, 2013 letter.) The Petitioners wanted to replace the Trustees with an independent third-party trustee. (App. 221, p. 183.) The Trustees responded that they would not resign, and they refused to provide copies of past leases. (Ex. 15, letter dated Sept. 11, 2013 and emails dated Sept. 12, 2013.) The Trustees further stated that they had no obligation to include a beneficiary "in any trust decision making" or to seek input concerning the leases. (*Id.*, email dated Sept. 12, 2013.) The Trustees negotiated the 2014 leases without input from the beneficiaries, and, on September 18, 2013, provided copies of the signed 2014 leases. (*Id.*, letter dated Sept. 18, 2013.)

The lease copies revealed that Lorin Schmidt was receiving a lower rate in 2014. (*Compare* App. 073-74 *with* App. 087-88.) They also showed that the Trustees had sharply increased the rent for all the tenants. In fact, on a per acre basis, the rent charged to the four Bialas tenants increased from $105 to $165, an increase of over 50%. (*See* Rent Table, *supra*.) Schmidt's rent remained lower, but his Douglas county land increased from $80 to $135, also over 50%, and his Hutchinson county rate increased even more dramatically: from $87.50 to $150, an increase of over 70%. The rate increase was not quite as large as it may appear, however, because the Trustees switched from charging rent based on gross acres to tillable acres. (*See, e.g.*, App. 073-74.) For example, in 2013, Willard Bialas

rented 160 acres at $105 per acre but in 2014 he rented 151.44 acres at $165 per acre.

Crop Year	Lorin & Barbara Schmidt Douglas /Hutchinson 160 acres/160 acres	DuWayne/Travis Bialas Douglas 200 acres	Craig & Stacey Bialas Hutchinson 160 acres	Willard Bialas Hutchinson 160 acres	Larry & Zita Bialas Hutchinson 80 acres
2009	$10,580/$11,560	$17,250[3]	$13,800	$13,170	$6,670
2010	$10,580/$11,560	$17,250	$13,800	$13,170	$6,670
2011	$10,580/$11,560	$17,250	$13,800	$13,170	$6,670
2012	$12,800/$14,000	$21,000	$16,800	$16,800	$8,400
2013	$12,800/$14,000	$21,000	$16,800	$16,800	$8,400
2014	$19,953/$21,384	$32,818.50	$26,037.00	$24,987.60	$12,462.45

(App. 064-134.) The change from gross acres to crop acres in 2014 cost the Trust thousands of dollars of income. (App. 268 ¶¶ 71-72.)

After the Trustees' refusal to disclose information about past years, to consult with the beneficiaries concerning 2014 rental rates, or to step down voluntarily, in November 2013, four of the five income beneficiaries, as well as Gene Loos, filed a Petition asking the Court to remove the Bormanns as Trustees and replace them with The First National Bank in Sioux Falls, an independent, third-party trustee. ®. 595, Petition, prayer for relief ¶ 4.) The Petitioners also sought to reopen the accountings for years 2009-12 due to material omissions in

[3]In 2009, Travis's land was covered by two leases for $10,350.00 and $6,900, which totaled $17,250.

the information presented to the Court, demanded copies of the leases for 2007-13, and asked for damages. (*Id.*, prayer for relief.)

On January 21, 2014, after a formal discovery request had been served, the Trustees provided copies of the 2007-12 leases in conjunction with their first motion for summary judgment. ®. 633, Aff. of Robert Bormann, Ex. A.) The Trustees initially took the position that they would not provide copies of the 2013 leases until the accounting for 2013 was presented to the Court for approval, but eventually produced "courtesy copies" on March 6, 2014 in conjunction with their response to the Petitioners' motion for summary judgment. (*See* App. 043 ¶ 1.)

The parties submitted cross-motions for summary judgment. The Petitioners conceded that they could not challenge court orders made before January 1, 2010, but contended that the orders approving the 2009-12 accountings were not conclusive pursuant to SDCL § 21-22-30 because the Trustees had omitted material information from their accounting reports, including Robert Bormann's relationship with Lorin Schmidt, the rates charged to each tenant, and had inaccurately reported that the Trust owned 680 acres of land, when it actually owned 920 acres. These omissions precluded the circuit court from being able to consider whether the relationship with Schmidt presented a conflict of interest or the fairness of the rental rates. The Petitioners requested that the Bormanns be removed and replaced by an independent trustee due to serious breaches of trust.

This request was supported by affidavits from four of the five income beneficiaries requesting appointment of a new and independent third-party trustee. ®. 839-845, Affidavits of Evelyn Lang, Gloria Loos, Virginia Binder, and Louis Hohn.)

After a hearing, the circuit court granted the Trustees' motion as to all accountings approved by the Court before January 1, 2010 based on SDCL § 21-22-27. (App. 001.) The circuit court otherwise denied both parties' motions for summary judgment. (*See id.*)

Both parties renewed their motions for summary judgment. In addition, the Trustees petitioned to have their 2013 accounting approved, and the Petitioners objected. On July 16, 2014, the circuit court granted the Trustees' motion for summary judgment concerning the 2009-12 accountings, concluding that they contained no material omissions. (App. 168, p. 11-12.) The circuit court reasoned that the omission of 240 acres from the accountings was inadvertent and that information in the vouchers, such as tax receipts, referred to all of the Trust property. (App. 168, p. 11.) The circuit court did not address the Trustees' failure during these years to disclose Robert Bormann's relationship with Schmidt, or their failure to disclose the rental rates charged to individual tenants. It denied summary judgment as to removal of the Trustees. (App. 168-69, p. 12-13.) The issues of the 2013 accounting and the trustees' removal were set for an evidentiary hearing on September 12, 2014.

Before the hearing, the Petitioners objected to the 2013 accounting in part because the Trustees had continued to lease to Schmidt at a preferential rate. ®. 977.) The Petitioners relied on both SDCL § 55-4-13 and *In re Estate of Stevenson*, 605 N.W.2d 818. (*Id.* ¶ 1.) The Trustees filed a motion to dismiss this objection. At the beginning of the September 12, 2014 hearing, the circuit court granted this motion. (App. 179, p. 15.) It concluded that, as a matter of law, Robert Bormann's relationship with Schmidt did not constitute a personal interest creating a conflict or self-dealing. (App. 179, p. 13-15.)

At the end of the evidentiary hearing, the circuit court denied the petition to remove the trustees. (App. 230-31, p. 218, 221-22.) It concluded that there had been no breaches of trust, and that their compensation was fair. (App. 230, p. 218.) It accepted and approved the 2013 accounting. (App. 006.)

Standard of Review

This Court reviews "de novo whether the moving party was entitled to summary judgment as a matter of law." *Amco Ins. Co. v. Employers Mut. Cas. Co.*, 2014 S.D. 20, ¶ 6 n.2, 845 N.W.2d 918, 920.

With regard to an evidentiary hearing, this Court reviews "'questions of fact under the clearly erroneous standard of review.'" *In re Estate of Moncur*, 2012 S.D. 17, ¶ 10, 812 N.W.2d 485, 487 (quoting *Weekley v. Prostrollo*, 2010 S.D. 13, ¶ 11 n.3, 778 N.W.2d 823, 827 n.3). But an error of law can prevent factual

findings from supporting a conclusion of law. *In re Estate of Stevenson*, 2000 S.D. 24, ¶ 7, 605 N.W.2d 818, 820 ("The issue is whether the findings support the conclusions of law. They do not because there is an error of law."). This Court reviews "purely legal questions de novo, giving no deference to the trial court's findings." *Estate of Moncur*, 2010 S.D. 17, ¶ 10, 812 N.W.2d at 487.

A court's decision whether to remove a trustee is reviewed for abuse of discretion. *See Estate of Unke*, 1998 S.D. 94, ¶ 29 & n.4, 583 N.W.2d 145, 150 & n.4; *see also* SDCL § 55-3-20.1. "'The abuse-of-discretion standard includes review to determine that the discretion was not guided by erroneous legal conclusions.'" *Pieper v. Pieper*, 2013 S.D. 98, ¶ 11, 841 N.W.2d 781, 785 (quoting *Koon v. United States*, 518 U.S. 81, 100 (1996)). "An abuse of discretion can simply be an error of law or it might denote a discretion exercised to an unjustified purpose, against reason and evidence." *Knodel v. Kassel Twp.*, 1998 S.D. 73, ¶ 6, 581 N.W.2d 504, 506.

Argument

1. The circuit court erred by determining as a matter of law that Bormann's relationship with Schmidt did not constitute self-dealing under *Estate of Stevenson*.

At the beginning of the evidentiary hearing concerning the 2013 accounting and removal of the Trustees, the circuit court ruled as a matter of law that Robert Bormann's relationship with Lorin Schmidt did not constitute self-dealing as

described in *Estate of Stevenson*. This was wrong. The circuit court erred because it mistakenly concluded that *Estate of Stevenson* concerned a single lease. An accurate reading of *Estate of Stevenson* would have lead the circuit court to reach the opposite conclusion: that as a matter of law Bormann's relationship was a breach of trust that permits the beneficiaries to void the lease with Schmidt.

Trustees are fiduciaries who must act "'wholly for the benefit of the trust.'" *In re Estate of Stevenson*, 2000 S.D. 24, ¶ 9, 605 N.W.2d 818, 820-21 (quoting *Willers v. Wettestad*, 510 N.W.2d 676, 680 (S.D. 1994)). This means they "'must act with utmost good faith and avoid any act of self-dealing that places [their] personal interest in conflict with [their] obligations to the beneficiaries.'" *Id.* at 821 (quoting *American State Bank v. Adkins*, 458 N.W.2d 807, 811 (S.D. 1990)). *Estate of Stevenson* concerned two separate leases of farm land owned by a trust. One lease was to the trustee's husband. The second lease was to the trustee's husband's cousin. The decision clearly states that two separate leases were at issue:

> On December 16, 1998, Tamara [the trustee] executed two new leases. One lease was to Tamara's husband, Randy Luke, for 456 acres and the second lease was to Randy's cousin, John Cap (Cap), for 312 acres. Cap's father, Steve Cap, is Randy's uncle and employs Randy as a farm laborer.

Id. ¶ 4, 605 N.W.2d at 820. *Estate of Stevenson* held that *both* leases constituted prohibited self-dealing and thus were void: "Article IX does not provide 'clear

and unmistakable language' authorizing the trustee to engage in self-dealing. Therefore, the leases to [the trustee's] husband *and* [trustee's husband's cousin] are void." *Id.* ¶ 17, 605 N.W.2d at 822 (emphasis added).

Estate of Stevenson shows that self-dealing encompasses more than transactions with spouses or blood relatives. It includes any transaction that places a trustee's personal interest in conflict with his obligations to the beneficiaries. The point is to prevent trustees from being in a position where they might be tempted not to act wholly in a trust's interest due to a personal interest, or, conversely, a position where the beneficiaries or third-parties might reasonably question whether the trustees acted wholly for the trust's benefit. *See NLRB v. Amax Coal Co.*, 453 U.S. 322, 329-30 (1981) ("To deter the trustee from all temptation and to prevent any possible injury to the beneficiary, the rule against a trustee dividing his loyalties must be enforced with 'uncompromising rigidity.'"); RESTATEMENT (SECOND) OF TRUSTS § 170, *comment c* ("The trustee violates his duty to the beneficiary not only where he purchases trust property for himself individually, but also where he has a personal interest in the purchase of such a substantial nature that it might affect his judgment in making the sale."). *Estate of Stevenson* held that a transaction with a trustee's spouse's cousin met this standard.

The relationship in this case is closer than *Estate of Stevenson*. Trustee Robert Bormann leased property to Lorin Schmidt. One of Robert Bormann's sons

married one of Schmidt's daughters. Although they are not blood relatives, Bormann and Schmidt have a personal tie through the marriage of their children and their shared grandchildren. It is eminently reasonable to question whether Robert Bormann's loyalties are divided when negotiating a farm lease with his grandson's grandpa. Consequently, as in *Estate of Stevenson*, the Schmidt leases may be voided by the beneficiaries.

The circuit court wrongly concluded as a matter of law that this relationship did not constitute self-dealing because it mistakenly believed *Estate of Stevenson* involved a single lease to a Trustee's husband and cousin:

> Petitioners object to the lease agreements for trust property made among the trustees and their family members and business associates in violation of SDCL 55-3-4 and *In re Stevenson*, 605 N.W.2d 818, South Dakota 2000, voiding ***a*** lease among trustee and trustee's husband and cousin. ***As I read the case, the trustee leased to her husband and cousin, not just the husband's cousin, but through the husband.***

(App. 179, p. 13 (emphasis added).) The emphasized language shows that the circuit court failed to recognize that *Estate of Stevenson* not only voided a lease to the trustee's husband, but also voided a separate lease to the trustee's husband's cousin. This caused the circuit court to assume that the relationship at issue in this case was more distant than the one at issue in *Estate of Stevenson,* when in reality the relationship here is closer.

In addition, the circuit court's comments at the end of the hearing show it further erred by assuming that beneficiaries can void a lease based on self-dealing only if they can show the conflict of interest affected the terms of the lease. In so doing, the circuit court applied the wrong legal standard to the lease's validity. *See Estate of Stevenson*, 2000 S.D. 24, ¶ 7, 605 N.W.2d at 820 (an error of law can prevent a factual findings from supporting conclusions of law). At the end of the hearing, the circuit court acknowledged the undisputed relationship between Robert Bormann and Schmidt. (App. 229, p. 214-15.) But instead of focusing on whether that relationship was sufficient to create reasonable questions whether Bormann's loyalties were divided, the circuit court attempted to discern whether the terms of the lease were affected by that relationship. (App. 229, p. 215-16.) It upheld the lease based on its determination that the rental rate was based on productivity of the land, rather than the personal relationship:

> We have an allegation that it was rented because of a family relationship. There is the presentation of figures that would attempt to show that there is a beneficial rental rate that was applied to that familial relationship, if you wish to characterize it that way. But the court does not find that to be true. The court, based upon the evidence, finds that the determination as to the value of the rental was calculated based upon the production in the years prior to the change.

(*Id.*) In so doing, the circuit court required Petitioners to prove that the trustee's personal relationship actually prejudiced the beneficiaries.

This is incorrect. *Estate of Stevenson* voided a farm lease based on the existence of a trustee's personal interest without inquiring whether the personal interest affected the rental rate. *See Estate of Stevenson*, 605 N.W.2d at 822, ¶ 17. This is consistent with the time-honored principle that the existence of a personal interest by the trustee is all that must be shown to void a transaction, and a transaction involving a conflict may not be upheld based on the contention that the trustee's personal interest had no effect on the transaction. *Amax Coal Co.*, 453 U.S. at 330 ("A fiduciary cannot contend 'that, although he had conflicting interests, he served his masters equally well or that his primary loyalty was not weakened by the pull of his secondary one.'") (quoting *Woods v. City Nat'l Bank & Trust Co.*, 312 U.S. 262, 269 (1941)); Am. Jur. 2d, *Trusts* § 350 ("Courts will not permit an investigation into the fairness or unfairness of such a transaction, or allow the trustee to show that the dealing was for the best interest of the beneficiaries."). Once it was established that Robert Bormann had a personal interest sufficient to raise reasonable questions about his ability to act wholly in the Trust's interest, the circuit court should have voided the lease as a matter of law.[4] *See Estate of Stevenson*, 605 N.W.2d at 821 (trustees "'must act with utmost good faith and avoid any act of self-dealing that places [their] personal interest in

[4]As discussed *infra*, the Petitioners acknowledge that the issue whether Bormann's personal interest affected the rent is relevant to the issue of damages.

conflict with [their] obligations to the beneficiaries.'") (quoting *American State Bank*, 458 N.W.2d at 811).

Furthermore, even if it were appropriate to consider the circumstances of the lease, the undisputed facts show that a conflict existed. Not only was Robert Bormann's relationship with Schmidt undisputed, it is also undisputed that Robert Bormann began leasing to Schmidt in crop year 1998, shortly after Bormann's son and Schmidt's daughter married. (App. 199, p. 96.) The accountings for 1998 and subsequent years, however, did not disclose to the beneficiaries or the Court that the new tenant was Schmidt or disclose the Schmidt family's relationship with Robert Bormann. It is also undisputed that the rent charged to Schmidt was lower than the Trustees charged to any other tenant. (*See* Rent Table, *supra*, pp. 40-41.)

Although the Trustees contended that this lower rate was based on productivity, there is no evidence that Schmidt's land is consistently less productive than the Bialas's land. Schmidt's Hutchinson county land actually has a higher soil rating than the land rented to Larry and Zita Bialas. (*See* App. 203, p. 111-12.) Even the 2003-06 data upon which the Bormanns supposedly relied shows that the Hutchinson county land was equally productive. (Ex. 104). Schmidt's Hutchinson county land produced a little less corn during 2003-06 (94.37 v. 97.88), but this was balanced by producing a little more soybeans (36.42 v. 32.56). (*Id.*) In fact, with respect to beans, Schmidt's Douglas county land

outperformed a number of the Bialas parcels in Hutchinson county. (App. 263, yield table.) In addition, in years 2012-14, the four Bialas tenants were charged the same rental rate, even though their parcels have a wide range of soil ratings and yields. (*See* Rent Table, *supra*, pp. 40-41; Ex. 112.) The undisputed facts provide no support for the contention that the rent charged to the various tenants was based on the relative productivity of the various parcels.

Although it should not matter whether the personal interest affected the transaction, the trustees' undisputed failure to disclose the relationship before entering into the lease and the lower rent charged confirms that reasonable questions exist whether Robert Bormann had divided loyalties. *See Estate of Stevenson*, 2000 S.D. 24, ¶ 7, 605 N.W.2d at 820 (when facts are not in dispute, this Court can determine legal questions de novo). The circuit court should have declared the lease void as a matter of law, and deemed this conflict a breach of the duty of loyalty to be considered when deciding whether the Trustees should be replaced by an independent trustee. The circuit court erred by ruling as a matter of law that Bormann did not engage in self-dealing under *Estate of Stevenson*.

2. The circuit court abused its discretion when it denied the request to replace the Bormanns with a neutral, independent trustee.

The circuit court concluded that there had been no breaches of responsibility as trustees by the Bormanns. (App. 230, p. 218.) It further concluded that the Bormanns' actions as trustees did not meet any of the

conditions set forth in SDCL § 55-3-20.1, and thus it did not have the power to remove the Bormanns. In the circumstances of this case, whether the Bormanns' acts met any of the conditions in Section 55-3-20.1 constituted a legal question. The circuit court erred by concluding that the Bormanns' acts did not constitute a serious breach of trust, and this legal error tainted its ultimate conclusion that it lacked the power to remove the Bormanns.

Section 55-3-20.1 states that a court "may remove a trustee if: (1) The trustee has committed a serious breach of trust." SDCL § 55-3-20.1. There are no South Dakota decisions discussing what constitutes a serious breach of trust. But this statutory language is taken directly from Section 706 of the Uniform Trust Code, and the comments to that section are helpful:

> A serious breach of trust may consist of a single act that causes significant harm or involves flagrant misconduct. A serious breach of trust may also consist of a series of smaller breaches, none of which individually justify removal when considered alone, but which do so when considered together. A particularly appropriate circumstance justifying removal of the trustee is a serious breach of the trustee's duty to keep the beneficiaries reasonably informed of the administration of the trust or to comply with a beneficiary's request for information as required by Section 813. Failure to comply with this duty may make it impossible for the beneficiaries to protect their interests. It may also mask more serious violations by the trustee.

U.T.C. § 706 (2000), comment on Subsection (b)(1).

As noted in the previous section, a trustee must "avoid any act of self-dealing that places [their] personal interest in conflict with [their] obligations to

the beneficiaries.'" *Estate of Stevenson*, 2000 S.D. 818, ¶ 9, 605 N.W.2d at 821 (quoting *American State Bank*, 458 N.W.2d at 811 (S.D. 1990)). By itself, failing to avoid a transaction tainted by a personal interest is a serious breach of trust because "a trustee's first duty as a fiduciary is to act in all things wholly for the benefit of the trust." *Willers v. Wettestad*, 510 N.W.2d 676, 680 (S.D. 1994). The circuit court, however, erroneously held as a matter of law that the Schmidt transaction did not constitute self-dealing under *Estate of Stevenson*. (App. 179, p. 15.) This error also affected the circuit court's exercise of its discretion whether to remove the Trustees. Because the circuit court believed that the transaction did not constitute self-dealing as a matter of law, it concluded that the Schmidt transaction did not weigh in favor of removing the Trustees. (App. 229, p. 214-16.)

The circuit court further erred, however, by not giving any weight to the Trustees' failure to disclose this conflict or the preferential rate given to Schmidt. The circuit court stated:

> One of the issues here is whether information was withheld or whether information was provided. The court, as far as I heard, never heard of any individual who would be representing the beneficiaries, whether current or contingent, coming forward, requesting the clerk to look at the file. Because that file is a public file, if it is requested, it can be examined.

(App. 228, p. 211.) In so ruling, the circuit court failed to recognize that it is not the beneficiaries' duty to search out potential conflicts. Rather, it is a trustee's duty "'to communicate to [the beneficiary] all material facts in connection with the

transaction which the trustee knows or should know.'" *Willers*, 510 N.W.2d at 680 (quoting RESTATEMENT (SECOND) OF TRUSTS § 170 (1959)). In this case, it would have been easy for the Trustees to have disclosed the relationship before entering into the first lease with Schmidt and to include copies of the leases with individual tenants as part of the individual accountings. In fact, during this litigation, the Trustees did attach copies of the 2013 leases to the 2013 accounting they filed in April 2014. (Ex. 113.)

Moreover, the Trustees not only failed to disclose the relationship before they began leasing property to Schmidt, they did not provide information on the 2007-13 rental rates when Gene Loos began requesting the information in early 2013. Trustees must "promptly respond to a qualified beneficiary's request for information related to the administration of the trust, unless the request is unreasonable under the circumstances." SDCL § 55-2-13. Gene Loos' request as a contingent remainder beneficiary and as POA for Gloria Loos, a current income beneficiary, for information on rental rates was eminently reasonable. The rent is the Trust's sole source of income. The beneficiaries have every right to know whether the Trustees are maximizing the Trust's income. Yet, as detailed in the Facts section, the Trustees resisted providing information on the 2007-2012 leases and rental rates for a year after Loos began asking for that information, and only provided that information after the Petitioners had begun this litigation and sent

formal discovery requests for the leases. The 2013 leases, moreover, were not provided until after the Petitioners moved for summary judgment on the issue of whether the Trustees are required to provide copies of the leases. (App. 043 ¶ 1.)

The Trustees have offered no justification for their failure to disclose their relationship with Schmidt or their delay in responding to Gene and Gloria Loos' request for information about the historical rental rates and copies of the leases. Whatever their motive, the breach of their duties to disclose all material facts and to promptly respond to reasonable requests for information masked the preferential treatment given to Schmidt, thus making it more difficult for the beneficiaries to protect their interests. *See* U.T.C. § 706, comment on Subsection (b)(1) ("Failure to comply with [the duty to keep beneficiaries reasonably informed] may make it impossible for the beneficiaries to protect their interests. It may also mask more serious violations by the trustee."). This type of breach is not just a serious breach, but a "particularly appropriate circumstance justifying removal of the trustee." *Id.*

Moreover, because the relationship with Schmidt and the content of the accountings provided to the beneficiaries were undisputed, whether the Schmidt transaction and its non-disclosure constitute a serious breach of trust is a legal question. *See Estate of Stevenson*, 2000 S.D. 24, ¶ 7, 605 N.W.2d at 820 ("Because the facts are not in dispute, we determine the legal questions de novo.") By failing to even recognize the Schmidt transaction was a breach of trust, or that

the Trustees had not promptly responded to reasonable requests for information, the circuit court reached an erroneous legal conclusion that guided its discretion whether to remove the Trustees, which is an abuse of discretion. *Pieper*, 2013 S.D. 98, ¶ 26, 841 N.W.2d at 788 ("That is an erroneous legal conclusion that guided the circuit court's discretion; therefore, the circuit court abused its discretion.").

In addition, courts may find a serious breach of trust based on the cumulative effect of less serious breaches. *See* U.T.C. § 706, comment on Subsection (b)(1) ("A serious breach of trust may also consist of a series of smaller breaches, none of which individually justify removal when considered alone, but which do so when considered together.") The circuit court failed to consider the cumulative effect of the following breaches of trust by the Trustees:

- The vouchers they filed with the Court for the Trust commingled records concerning the Trustees' other personal and business matters. (App. 194-95, p. 75-80.)
- They made references in proposed orders to documents that were never served on any party and were not filed with the Court when the proposed order was submitted. (Ex. 2; App. 194, p. 73-75.)
- They missed at least two payments, causing the Trust to incur late payment charges, but did not reimburse the Trust. (Ex. 12; App. 196-97, p. 83-85.)
- For many years, the accounting they provided to the Court listed only 680 acres of the 920 acres owned by the Trust. (E.g., Ex. 3; App. 053-54 ¶ 3.)

- For many years, they obtained liability insurance only for 680 acres. (App. 192, p. 67-68; Ex. 13.)

- For many years, they have deposited the Trust's funds in the bank they own and receive dividends from, (App. 191, 195, 210, p. 63, 77-78, 140), thereby using trust property for their own profit. SDCL § 55-2-2.

- They leased trust property only to customers of the bank they own. (App. 184, p. 33-34.)

- The Trustees did not serve copies of the accounting information on any of the contingent remainder beneficiaries as required by SDCL Ch. 21-22 until the 2013 accounting period. (App. 043 ¶ 5.)

The circuit court erred in its approach by not considering whether the cumulative effect of all the breaches discussed in this section justified removal of the Trustees. These legal errors clearly affected the circuit court's ultimate conclusion that it did not have the power to remove the Trustees in these circumstances. (App. 230-31, p. 218-22.) This Court should hold that the cumulative effect of all the breaches constitutes a serious breach of trust warranting removal as a matter of law, or, at a minimum, clarify that the Schmidt transaction and failure to promptly provide information about the 2007-13 rental rates and leases were serious breaches of trust, and remand to the circuit court with an order to remove the Trustees.

3. The circuit court erred by ruling as a matter of law that no material omissions occurred for past accountings.

The circuit court granted summary judgment concerning the issue whether the accountings for 2009-12 omitted any material information. (App. 003.) The circuit court erred by focusing on whether the omissions were inadvertent rather than material, and by failing to even consider whether the Schmidt transaction was material. (App. 168-69.)

Section 21-22-30 provides that an accounting for a court supervised trust is conclusive and a trustee is released from liability "absent fraud, intentional misrepresentation, or material omission." SDCL § 21-22-30. Although Chapter 21-22 does not define "material omission," its meaning can be deduced from the provisions setting forth the trustee's duty to give an account and the court's duty to examine that report. Section 21-22-14 requires a trustee's annual report to show "in detail his receipts, disbursements, and acts during the year." SDCL 21-22-14. Section 21-22-22 in turn requires the supervising court to "examine all reports and accounts filed, regardless of whether or not objections are made thereto, and [the court] shall also consider and pass upon all acts of the trustee, regardless of whether any question is raised with reference thereto." SDCL § 21-22-22. Similarly, Section 21-22-23 precludes the court from approving an accounting until the court has "made a detailed examination of the items and satisfied itself sufficiently to render its own judgment thereon, that the report is in all things true

and complete, and the acts done have been in compliance with the trust and for the advantage and best interests thereof." SDCL § 21-22-23. A material omission thus is an omission that prevents a court from being able to satisfy its statutory duty to make a detailed examination of the trustee's actions during the past year and determine whether the accounting is true and complete and that all of the trustee's actions were in the best interests of the trust.

The omissions in this case easily meet the standard of materiality. First, it is undisputed that all of the 2009-12 accountings indicated that the Trust owned only 680 acres of land and did not include any leases. The Trust's primary asset is the 920 acres of farmland, so omitting 240 of those acres means that a significant percentage of the Trust's assets were missing from the accounting. Similarly, because this is the primary asset, negotiating new leases is by far the most significant act that the Trustees perform each year. Omitting copies of these leases, or even the relevant information from them such as the identity of the tenant and rent charged, means that the accounting did not inform the circuit court concerning the Trustees' most important transactions. How then could the circuit court possibly have "rendered its own judgment" that the Trustees' actions were in the best interest of the Trust?

For example, the omission of 240 out of 920 acres combined with the failure to include the leases or even basic information from the leases precluded

the court from rendering its own judgment that the rental rates charged to the individual tenants were in the Trust's best interest. This is particularly important here because it is also undisputed that none of the accountings disclosed the connection between Robert Bormann and Schmidt or that Schmidt was receiving a more favorable rental rate than the other tenants. Again, this means it is impossible for the circuit court to have "rendered its own judgment" whether that relationship constituted self-dealing and whether it was in the Trust's best interest to charge Schmidt a lower rental rate.

None of the reasons for the omission offered by the Trustees or the circuit court justify the failure to include this information. The circuit court focused on how the Trustees did not intend to omit 240 acres from the accountings. But the motive for the omission does not affect its materiality. Even if the omission were innocent, the combination of listing only 680 acres and omitting rental information was misleading because it made the rental rates appear higher than they actually were. The Trustees argue that information in the vouchers such as tax records could have enabled the circuit court to deduce that there were 920 acres in the Trust. There are multiple problems with this assertion, one of which is that there is no evidence the vouchers disclosed Robert Bormann's relationship with Schmidt or the preferential rental rate he received.

In addition, to the extent there was relevant information contained in the vouchers, it does not cure an omission in the accountings. The vouchers were just a loose collection of documents in an envelope. In contrast, the accounting is "a verified report." SDCL § 21-22-14. It must be sent to all beneficiaries and their attorneys. SDCL § 21-22-18. The information in the vouchers was neither verified nor was it served upon the beneficiaries. Moreover, the docket shows that the file dates on most of the vouchers are months after the court order approving the accounting, so it has not even been established that the circuit court had access to the information in the vouchers before it approved the accountings. Nothing in the summary judgment record even remotely suggests that the Trustees satisfied their duty to report all material information concerning their acts so that the circuit court could independently review the Schmidt lease or the rates charged to Schmidt and the other tenants.

The entire point of a court supervised trust is to create an additional source of accountability for a trustee's actions. This independent review is particularly important where, as here, the beneficiaries are elderly persons who need help protecting their own interests. By not including rental rates, not identifying individual tenants, and not disclosing the circumstances of the Schmidt transaction, the Trustees completely prevented the circuit court from being able to provide an independent review of these issues. This is a material omission by any measure.

Moreover, it is more than fair to hold trustees to a high standard when determining whether they have made a "material omission" in an annual accounting because court approval of the accounting insulates the trustees from liability. SDCL § 21-22-30. A trustee should not receive the immunity associated with circuit court review unless the trustee has truly presented all material facts concerning the prior year's transactions for the circuit court to review. The circuit court erred when it granted the Trustees' motion for summary judgment and denied the Petitioners' cross-motion for summary judgment on this issue. In these circumstances, it should have held that the omissions were material as a matter of law. This Court should reverse the circuit court's summary judgment and hold that the omissions were material.

4. As a remedy for the breaches of trust related to the Schmidt transaction, this Court should hold that the Schmidt leases are void, the Trustees should be removed, and the Petitioners may recover damages caused by the Schmidt leases.

Because the circuit court did not find the Schmidt transaction to involve self-dealing and did not find any material omissions, it did not reach the issue of remedy. As discussed above, the circuit court should have granted the Petitioners' motion for summary judgment. Petitioners request this Court to hold that the Trustees should be removed and the circuit court instructed to appoint an appropriate independent third-party trustee on remand. The Petitioners also request that this Court hold the Schmidt leases are void as a matter of law for years

2009-14. It is not possible to go back in time and lease the land to someone else or to charge Schmidt the same rent as the Bialas tenants. But the Trustees can be held personally liable for damages resulting from breaches of duty. *Willers v. Wettestad*, 510 N.W.2d 676, 680-81 (S.D. 1994) ("If the trustee commits a breach of trust, he is chargeable with any loss or depreciation in value of the trust estate resulting from the breach of trust."). Indeed, Section 21-22-26 requires trustees to be held liable for damages resulting from breaches of Chapter 21-22. SDCL § 21-22-26 (trustees who do not comply with Ch. 21-22 "shall be liable to any beneficiary for all damages sustained by such beneficiary resulting from such noncompliance").

Here, the rent paid by the Bialas tenants establishes that the Trust land could have produced at least the rent charged to them. The simplest measure of damage thus is the difference between the rent charged to Schmidt and the rate charged to the Bialas tenants. For years when the Bialas tenants were charged different rates, the Petitioners are willing to use the lowest rate charged to a Bialas tenant, which was Larry and Zita Bialas. It is particularly fair to use the rent paid by Larry and Zita Bialas because the soil rating of their land is lower than Schmidt's Hutchinson county land and virtually the same as his Douglas county land. This yields the following damages for Douglas county land:

Crop Year	Lorin & Barbara Schmidt Douglas 160 acres rate per acre	Larry & Zita Bialas Hutchinson 80 acres rate per acre	Difference in rent per acre	Damages (difference X acres leased)
2009	$66.13	$82.31	$16.18	$2,588.80
2010	$66.13	$82.31	$16.18	$2,588.80
2011	$66.13	$82.31	$16.18	$2,588.80
2012	$80	$105	$25	$4,000
2013	$80	$105	$25	$4,000
2014	$135	$165	$30	$4,800
			Douglas Total:	$20,566.40

And the following damages for Hutchinson county land:

Crop Year	Lorin & Barbara Schmidt Hutchinson 160 acres rate per acre	Larry & Zita Bialas Hutchinson 80 acres rate per acre	Difference in rent per acre	Damages (difference X acres leased)
2009	$72.25	$82.31	$10.06	$1,609.60
2010	$72.25	$82.31	$10.06	$1,609.60
2011	$72.25	$82.31	$10.06	$1,609.60
2012	$87.50	$105	$17.50	$2,800
2013	$87.50	$105	$17.50	$2,800
2014	$150	$165	$15	$2,400
			Hutchinson Total:	$12,828.80
			Total both counties	$33,395.20

This results in total damages of $33,395.20. In addition, pursuant to SDCL § 21-22-26, the Trustees are required to forfeit their compensation for 2009-13 for their unjustified omissions of material information concerning their relationship with Schmidt and the preferential rate provided to him. Their fees for 2009-13 are listed on the exhibit attached to each of their accountings and total $26,000.00. (App. 138, 141, 145, 149 & 153.)

Conclusion

Serving as a trustee is a high calling with high standards. As in this case, trustees often handle money for people who cannot protect themselves as well as the average adult. It is therefore critical for trustees to avoid placing themselves in a conflicted position and to disclose all material facts to the courts supervising them. Here, the Trustees failed to meet these high standards by entering into a transaction tainted by a personal interest and by not disclosing the material facts concerning that transaction to the circuit court supervising them. Moreover, when the beneficiaries began to investigate the Trustees' actions, they compounded their breach by failing to promptly provide the relevant information. The circuit court erred by holding as a matter of law that no breaches of duty occurred. Petitioners respectfully request that this Court reverse the circuit court and hold that the Schmidt transaction was a serious breach of trust that entitles the beneficiaries to have the Trustees removed, to void the Schmidt leases, and to recover the

difference between the Schmidt lease and the lowest rate charged to the other tenants.

Dated this 12th day of January, 2015.

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Certificate of Compliance

In accordance with SDCL § 15-26A-66(b)(4), I certify that this brief complies with the requirements set forth in the South Dakota Codified Laws. This brief was prepared using WordPerfect X6, and contains 9,286 words excluding the table of contents, table of cases, jurisdictional statement, statement of legal issues and certificate of counsel. I have relied on the word count of the word-processing program to prepare this certificate.

Dated this 12th day of January, 2015.

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Certificate of Service

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Appendix

Orders

Statements of Undisputed Material Facts (SUMF) and Responses

Leases

Sources: Aff. of Robert Bormann, Ex. A (2009-12); Ex. 105-110 (2013); Ex. 19 (2014).

Accountings

Hearing Transcripts

IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

No. 27273

GLORIA LOOS, ESTATE OF LOUIS HOHN, EVELYN LANG,
VIRGINIA BINDER, and GENE LOOS,

Appellants,

vs.

ROBERT BORMANN and PAUL BORMANN,

Appellees.

Appeal from the Circuit Court
First Judicial Circuit
Hutchinson County, South Dakota

The Honorable Glen Eng and the Honorable Patrick Smith

BRIEF OF APPELLEES

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Notice of Appeal filed November 26, 2014

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PRELIMINARY STATEMENT

The record below is cited as "R". Hearing Exhibits from the September 12, 2014, evidentiary hearing will be designated as "HE" followed by the applicable exhibit number. References to the Appendix will be referred to as "App." along with the applicable page number.

JURISDICTIONAL STATEMENT

Petitioners Gloria Loos, the Estate of Louis Hohn, Evelyn Lang, Virginia Binder, and Gene Loos ("Petitioners") appeal from several orders regarding the Joseph Baumgart Trust ("Trust"). They are an Order and Judgment allowing and approving Trustees' Robert Bormann ("Bob") and Paul Bormann ("Paul" and, collectively, "Trustees") Annual Account and Dismissing Objections filed October 14, 2014 (R 1012-15); Order on Renewed Motions for Summary Judgment (R 952); Order on Motions for Summary Judgment (R 875-76); Decree of Settlement of Annual Account and Report of Trustees filed February 4, 2013 (R 588-90); Decree of Settlement of Annual Account and Report of Trustees filed January 24, 2012 (R 575-77); Decree of Settlement of Annual Account and Report of Trustees filed January 25, 2011 (R 562-64); and Decree of Settlement of Annual Account and Report of Trustees filed January 26, 2010. (R 549-51.) Notice of Entry of the Orders was given on October 29, 2014. (R 1016-1038.) Notice of Appeal was filed on November 26, 2014. (R 1039-40.)

STATEMENT OF THE ISSUES

1. Whether Trustees' leasing Trust property to Lorin Schmidt constitutes self-dealing?

   The Circuit Court determined that leasing Trust property to Lorin Schmidt did not constitute self-dealing as Trustee Bob Bormann and Lorin Schmidt are not related nor did the terms of the leases between Lorin Schmidt and the Trust constitute self-dealing.

- SDCL § 55-4-13
- SDCL § 55-4-1
- *In re Estate of Stevenson*, 2000 S.D. 24, 605 N.W.2d 818

2. Whether Trustees breached any fiduciary duties and whether Trustees should be removed?

   The Circuit Court, after a full evidentiary hearing, concluded Trustees did not breach any fiduciary duties and should not be removed.

   - SDCL § 55-3-20.1
   - *In re Betty A. Luhrs Trust*, 443 N.W.2d 646 (S.D. 1989)
   - *In re Guardianship of Larson,* 1998 S.D. 51, 579 N.W.2d 24
   - *In re Estate of Wallbaum*, 2012 S.D. 18, 813 N.W.2d 111

3. Whether the Circuit Court properly granted summary judgment to Trustees and denied Petitioners' motion for summary judgment regarding Petitioners' claims to reopen the 2009 through 2012 accountings?

   After a full review of the relevant evidence, the Circuit Court held that the 2009 through 2012 accountings were proper and that the inadvertent non-listing of two descriptions of real property did not void the determination that the approval of the accountings was final.

   - SDCL § 21-22-30

STATEMENT OF THE CASE

This Trust has been under Court supervision by the First Judicial Circuit, Hutchinson County, since Joseph Baumgart's ("Joseph" or "Settlor") death in 1978. (R 1-17.) Its corpus consists of approximately 920 acres of farmland in Hutchinson County and Douglas County, of which 874.03 acres are tillable. (HE 111.) Joseph personally selected the individuals he wanted to serve as trustees of his Trust. (HE 103.) The Trustees' past annual accountings were approved by the Circuit Court pursuant to SDCL Ch. 21-22 without objection from any of the Trust's beneficiaries. (*See generally* Register of Actions.)

The income beneficiaries of the Trust are Joseph's living nieces and nephews. (HE 103.) Upon the death of all of Joseph's nieces and nephews, the Trust property will be converted into cash and distributed in equal shares to Joseph's living great-nieces and great-nephews. (*Id.*) Those great-nieces and great-nephews are entitled to nothing under the Trust until the last of Joseph's nieces and nephews passes away. (*Id.*)

Petitioners Gloria Loos, Evelyn Lang, and Virginia Binder are three of Joseph's elderly nieces who currently receive income from the Trust. (R 595.) Petitioner Louis Hohn has since passed away. (*See* Suggestion of Death and Motion for Substitution of Party.) Joseph has another living niece who did not join in Petitioners' claims. (App. 75-76, 82, p. 196-97, 221.) Gene Loos is a great-nephew of Joseph and is entitled to nothing under the Trust unless he survives his mother and aunts. (R 595; HE 103.)

On November 19, 2013, Petitioners filed a Petition to Reopen Accountings, Request for Information, and Removal of Trustees and Appointment of Successor Trustee on the Ground of Fraud, Material Omission or Misrepresentation ("the Petition") seeking to reopen the Court-approved accountings for 2007 to 2012. (R 595-13.) They claimed Trustees rented the Trust farmland at below market value, engaged in self-dealing by renting the farmland to relatives and/or customers of Farmers State Bank, and refused to provide copies of the farm leases for 2007 through 2012 to Gene Loos. (*Id.*)

On April 30, 2014, the Circuit Court, the Hon. Glen Eng presiding, granted Trustees' motion for summary judgment as to all accountings approved prior to January 1, 2010, based upon SDCL § 21-22-27. (R 875-76.) It denied the remainder of the parties' cross-motions. (*Id.*) Both parties renewed their motions for summary judgment. The Circuit Court then granted summary judgment to Trustees on the remainder of

Petitioners' Petition after considering the submissions and arguments from both sides. (R 952.) However, the Court left open the question of removal because Petitioners planned to file objections to the 2013 accounting on similar grounds. (*Id.*)

Thereafter, Trustees sought approval of their 2013 accounting. (R 953-72.) Petitioners filed Objections to Trustees' Accounting (2013). (R 975-76.) Petitioners objected to the lease agreements between the Trust and one tenant, Lorin Schmidt, claiming Trustee Bob Bormann and Schmidt are relatives because Bob's son is married to one of Schmidt's daughters. (R 975.) They also claimed all of the Trust's farmland was rented below market value, and that the Trustees' compensation was unreasonable. (*Id.*) Petitioners sought removal of Trustees. (App. 29, p. 9.)

On September 12, 2014, Judge Eng conducted an evidentiary hearing, where live testimony and a number of exhibits were offered by the parties. After hearing the evidence and judging the credibility of the witnesses, Judge Eng rejected Petitioners' contention that Trustees committed self-dealing by leasing Trust property to Schmidt because Bob and Schmidt are not relatives. (App. 30, p. 13-16.) He also determined that Petitioners' proposed rental rates were unsupportable and that the Trustees did not rent the farmland at unreasonable rates or give preferential treatment to Schmidt. (App. 80-81, p. 213-18.) Judge Eng also rejected Petitioners' contention that the Court did not have all necessary information for the years it approved past accountings. (App. 81-82, p. 220-21.) He denied Petitioners' request for removal of Trustees and found their compensation was reasonable. (App. 81-82, p. 218-222.)

On October 14, 2014, the Circuit Court entered an Order and Judgment Allowing and Approving Trustees' Annual Account and Report and Dismissing Objections,

incorporating into the Order its Findings of Fact and Conclusions of Law stated orally and recorded in open court following the close of the evidence pursuant to SDCL § 15-6-52(a). (R 1012-15.) This appeal followed.

STATEMENT OF FACTS

1. Joseph Baumgart's Trust

Joseph executed his Last Will & Testament on July 13, 1976. (HE 103.) His will established a trust whereby the residue of his estate, which consisted of farmland in Hutchinson and Douglas Counties, would be held in trust by his attorney, Henry Horstman and his banker, Vern Bormann. (*Id.*)

The Trust Instrument instructs the Trustees to pay the income from the Trust to Joseph's living nieces and nephews for as long as at least one niece or nephew lives. (*Id.*) Upon the passing of the last niece or nephew, the Trust Instrument directs the Trustees to liquidate the Trust's principal and distribute the assets to the Settlor's then living grand-nieces and grand-nephews. (*Id.*) No grand-niece or grand-nephew is entitled to any distribution from the Trust until the Settlor's last niece or nephew has died. (*Id.*) Joseph included strong exculpatory language in the Trust Instrument, expressly absolving Trustees from any "loss sustained through an error of judgment" and provided that the Trustees would only be liable for a loss caused by "willful default." (*Id.*)

As successor trustees, Joseph specifically named the current Trustees, Paul and Bob Bormann. Bob was appointed as a co-trustee after the resignation of Henry Horstman in 1989 and Paul was appointed as a co-trustee after the death of Vern Bormann, the Trustees' father. (R 217-18, 280-81.) For several generations, the Bormann family has owned Farmers State Bank, which has its main branch in Parkston, S.D. (App. 31, p. 20.) Joseph trusted Vern Bormann and visited him several times a

week in the bank. (App. 32, p. 21.)

2. Trust Property

During his lifetime, Joseph leased the land owned by the Trust to two primary families. He leased approximately 583.67 acres of the tillable land now owned by the Trust to the family of Fritz Bialas (the "Bialas Land"). The remaining 290.36 acres consist of two parcels, one in Douglas County and one in Hutchinson County. (HE 111.) The Thuringer family rented the parcel in Douglas County until their retirement while Herbert Koster rented the Hutchinson County parcel. (App. 33, 35, p. 25, 33.) When Joseph executed the Trust Instrument, all tenants were customers of Farmers State Bank. (App. 33, p. 25.) Similarly, all of the current tenants of the Trust farmland are customers of the bank. (App. 35, p. 34.) Until approximately 1999, Farmers State Bank was the only bank in Parkston. (*Id.*)

3. Settlor's Intent for Renting his Trust Property

When Joseph first started discussing what to do with his land when he died, he consulted with Vern. (App. 32, p. 21.) Bob took part in some of those conversations. (*Id.*) On one occasion, Joseph called Bob into Vern's office at the bank and specifically asked Bob if he would serve as a successor trustee. (App. 32, p. 23.) Joseph knew the Trust would exist for a number of years, that Bob was involved in farming during the summers and that Bob dealt with agricultural matters at the bank. (*Id.*)

Joseph made clear he wanted the Bialas family to continue renting land from the Trust after his passing as he trusted their farming practices and believed in them. They were good stewards of the land. (App. 32-33, p. 22, 25.) Fritz Bialas and Joseph were very good friends, so much so that Joseph named Fritz's issue as the contingent beneficiaries of the Trust in the event his nieces and nephews have no living issue when

the last niece or nephew passes away. (App. 32-33, p. 24-25.)

Joseph also made clear that he did not want his nephews and nieces, including Petitioners, to get his land. (App. 32, p. 22.) He wanted members of the Bormann family to serve as trustees until the land was liquidated and sold off for the benefit of the contingent remaindermen. (App. 32, p. 24.) Joseph insisted the tenants of the land practice good husbandry as he wanted to ensure his property was well-maintained. (App. 32-33, p. 24, 26.)

Today, the Bialas Land continues to be rented to descendants of Fritz Bialas, just as Joseph did when he was alive and as he intended upon his death. (App.34-35, p. 32-33; HE 107-110.) The remaining parcel in Douglas County continued to be leased by the Thuringer family and until they ceased farming in the 1990s. (App. 35, p. 33.) Herbert Koster rented the remaining Hutchinson County parcel until his retirement, followed by an additional family until their retirement, and all lived in close proximity to the land. (App. 33, 25; R 628.)

Currently, the Thuringer parcel in Douglas County and the parcel previously rented to Herbert Koster in Hutchinson County are leased to Lorin Schmidt, a farmer who lives close to the properties. (App. 35, p. 33, HE 105-106). Prior to Schmidt renting the Douglas County ground from the Trust, Jim Thuringer rented the ground. (App. 51, p. 97-98.) Contrary to Petitioners' insinuations, Trustees did not terminate Jim Thuringer's lease in order to rent the land to Schmidt. Rather, Thuringer informed Trustees he was quitting farming and did not want to lease the land anymore. (App. 35, 60, p. 33, 135.) Therefore, Trustees sent him written notice of lease termination, as directed by their attorney. (App. 60, p. 135.) Trustees rented the land to Schmidt as he

had previously been the only farmer to approach them about renting that ground. (App. 51, 62, p. 98, 141-42.) Trustees chose to rent to him due to his good farming practices, as Joseph directed. (App. 51, p. 98.)

One of Schmidt's daughters is married to one of Bob's sons. (App. 51, p. 97.) Bob and Schmidt are not related by consanguinity or affinity. (App. 80, p. 215.) Other than this attenuated connection, there is no other relationship between Trustees or any of the tenants of the Trust property. (App. 51, p. 98.) Moreover, Schmidt originally contacted Paul, not Bob, about renting the land a couple years before it became available and years prior to the marriage between Bob's son and Schmidt's daughter. (App. 35, 51, 62, p. 33, 98, 141-42.)

All of the Trust land is located in the westernmost portion of Hutchinson County and the easternmost portion of Douglas County. (App. 35, p. 34-35.) The James River divides Hutchinson County into an eastern and western half and Douglas County is west of Hutchinson. (*Id.*) The land on the western side of the James River in Hutchinson County is less fertile than the land on the east side of the county. (*Id.*) The Douglas County land is less fertile as well, given its location. (*Id.*, p. 35.)

4. Trustees Establish Cash Rent Leases at Request of Petitioners

For most of the Trust's existence, Trustees rented the Trust farmland on a share-crop basis, meaning the Trust would receive a fixed percentage of the profits earned by the tenant at harvest. (App. 36, p. 37.) For the crop year 2007, two of the beneficiaries, including deceased Petitioner Louis Hohn, demanded the Trustees convert to cash rent leases to try and stabilize income. (*Id.*, p. 38.)

The Trustees acquiesced in this demand, and beginning in 2007, the leases were converted to cash rent (*See, e.g.*, HE 105-110.) A multitude of factors were used to

determine the rent rates, including:

- Trustees' experience living in the area most of their lives;
- rent prices in the vicinity of the Trust land;
- Bob's 40 years of experience in agricultural lending;
- historical production of the Trust land;
- soil quality;
- topography;
- drainage issues; and
- USDA documentation of prior rental rates in the two counties.

(App. 35-37, 40, p. 35-42, 53; HE 112, 104, 102, 101.)

As Judge Eng noted in his ruling, Trustees have different obligations to income beneficiaries and contingent remaindermen. (App. 80, p. 213.) As a result, Trustees must evaluate whether the tenants of the property practice good husbandry and farm the land appropriately to ensure it will result in a maximum dollar value for Joseph's great-grandnieces and nephews when it is eventually sold, while still ensuring reasonable rental rates to produce Trust income. (App. 38, p. 45-47.) Blindly renting the land to the highest bidder leads to farming practices that destroy and deplete the land causing damage to the Trust property, which violates Joseph's intent. (App. 40, p. 53-54.) Further, these same type of farmers demand longer leases, which are impossible due to the age of the income beneficiaries and the terms of the Trust. (App. 81, p. 217.)

Trustees have been very satisfied with the good farming practices used by the tenants over the years. (App. 38, p. 47-48.) No concerns exist regarding timely receipt of rental payments, tenants walking away from their leases, or tenants destroying the land

with hard farming practices. (*Id.*) In fact, the tenants have improved the property for its inevitable sale, including ditching, trenching, weed control, maintaining fences, and removing old buildings and foundations to increase tillable acreage. (App. 38-39, p. 48-50.) The husbandry and care of the land over the years has vastly improved it and will result in a maximum dollar value for the great-grandnieces and nephews when it is eventually sold. (App. 39, p. 50.)

ARGUMENT

*1. **Standards of Review.***

The issues in this case have different standards of review. While Petitioners contend all the issues are governed by the *de novo* standard, that is incorrect.

First, the Circuit Court's determination that leasing Trust property to Schmidt was not self-dealing raises a mixed question of fact and law, governed by the clearly erroneous standard. *See In re Dorsey & Whitney Trust Co.*, 2001 S.D. 35, ¶ 6, 623 N.W.2d 468, 471 (citation omitted) (a mixed question of law and fact includes one in which "the historical facts are admitted or established, the rule of law is undisputed, and the issue is whether the rule of law as applied to the established facts is or is not favorably satisfied.") The nature of the inquiry determines the standard of review. *Huether v. Mihm Transp. Co.*, 2014 S.D. 93, ¶ 14, 857 N.W.2d 854, 859-60 (citation omitted). As this Court has stated,

> [i]f application of the rule of law to the facts requires an inquiry that is 'essentially factual'—one that is founded 'on the application of the fact-finding tribunal's experience with the mainsprings of human conduct'—the concerns of judicial administration will favor the [circuit] court, and

> the [circuit] court's determination should be classified as one of fact reviewable under the clearly erroneous standard.

Id. (quoting *Darling v. W. River Masonry, Inc.*, 2010 S.D. 4, ¶ 10, 777 N.W.2d 363, 366).

Here, the law regarding self-dealing is established by SDCL § 55-4-13. Petitioners argue Trustees violated this statute by renting land to Schmidt. Whether the relationship between Trustees and Schmidt constitutes one of self-dealing is a mixed question, hinging on factual determinations. Therefore, the Court's determination is reviewed under the clearly erroneous standard.

Second, the Circuit Court's determination that Trustees did not breach any fiduciary duties is reviewed under the clearly erroneous standard because that is a question of fact. *In re Estate of Moncur*, 2012 S.D. 17, ¶ 10, 812 N.W.2d 485, 487 (citations omitted). The question is not whether this Court would have made the same findings the trial court did. *Stockwell v. Stockwell*, 2010 S.D. 79, ¶ 16, 790 N.W.2d 52, 59 (citation omitted). Rather, the Circuit Court's findings of fact are clearly erroneous only "when a complete review of the evidence leaves this Court with a definite and firm conviction that a mistake has been made." *In re Conservatorship of Gaaskjolen*, 2014 S.D. 10, ¶ 9, 844 N.W.2d 99, 101 (citations omitted).

Third, the Circuit Court's determination that removal of Trustees was not warranted is reviewed under the abuse of discretion standard. *Estate of Unke*, 1998 S.D. 94, ¶¶ 26 & 29, 583 N.W.2d 145, 150 n. 4. "Abuse of discretion is the most deferential standard of review available with the exception of no review at all." *In re S.D. Microsoft Antitrust Litig.*, 2003 S.D. 19, ¶ 27, 657 N.W.2d 668, 678 (citations omitted).

Finally, this Court's standard of review regarding summary judgment is well-settled. Summary judgment is proper where the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. SDCL § 15-6-56(c). *See also Law Capital, Inc. v. Kettering*, 2013 S.D. 66, ¶ 10, 836 N.W.2d 642, 645 (citations omitted). "Summary judgment is a preferred process to dispose of meritless claims." *Horne v. Crozier*, 1997 S.D. 65, ¶ 5, 565 N.W.2d 50, 52 (citations omitted).

2. The Circuit Court correctly determined the leasing of Trust real property to Lorin Schmidt did not constitute self-dealing as Trustees did not personally benefit in any way from the leases.

A. Trustee Bob Bormann and Lorin Schmidt are not relatives.

Petitioners argue the Circuit Court incorrectly ruled that Trustee Bob Bormann was not related to Lorin Schmidt and that renting land to Schmidt did not constitute self-dealing. Petitioners' argument lacks merit.

The categories of persons to whom a trustee may not lease trust property are expressly defined in SDCL § 55-4-13. It precludes a trustee from leasing trust property to a relative, unless expressly authorized to do so by the trust instrument. SDCL § 55-4-1 defines "relative" to mean "a spouse, ancestor, descendant, brother, or sister." Bob and Schmidt are none of these things so no self-dealing could exist. The Circuit Court should be affirmed.

Petitioners ignore these unambiguous statutes and instead rely solely upon *In re Estate of Stevenson*, 2000 S.D. 24, 605 N.W.2d 818, claiming it somehow changes the rules adopted by the Legislature. Petitioners are wrong on both fronts. *Stevenson* did not

expand the above-cited statutes. Even if it did, the Schmidt leases still complied with Petitioners' reading of *Stevenson*.

In *Stevenson*, the trustee executed two leases for rental of farm property, one to her husband and one to her husband's cousin. 2000 S.D. 24, ¶ 4, 605 N.W.2d 818, 820. The primary beneficiary of the trust sought to void the leases arguing the trustee committed self-dealing by leasing land to relatives. *Id.* at ¶ 5. This Court concluded the trust instrument did not authorize the trustee to lease property to herself, her husband, or a relative and voided the leases. *Id.* at ¶ 17, 605 N.W.2d at 822. The focus of the inquiry was the language in the trust instrument, not the statute, as it is here.

Petitioners contend the relationship between Bob and Schmidt is even closer than the relationships in *Stevenson* because one of Bob's sons is married to one of Schmidt's daughters. (Petitioners' Brief at 22-23.) This is plainly incorrect as Bob and Schmidt are not related in any manner recognized by law. People are related by consanguinity, *i.e.*, "by blood," or by affinity, *i.e.*, "by marriage."

> "Affinity" is defined as a legal relationship which arises as the result of marriage between each spouse and the consanguinal relatives of the other. Each spouse is related by affinity to the blood relations of the other in the same degrees as the other, *but the blood relations of one spouse are not, by reason of marriage, related by affinity to the blood relations of the other*[.]

41 Am. Jur. 2d *Husband & Wife*, § 4 (emphasis added).

Petitioners fail to comprehend the trustee in *Stevenson* was related by affinity to her husband's cousin. The current situation is completely different. Bob and Schmidt are not related by blood or affinity. Contrary to Petitioners' assertion, Bob and Schmidt are not closer relatives than the trustee and husband's cousin in *Stevenson* as they are not related at all. Thus, even if *Stevenson* expanded the class of prohibited leases by trustees,

the leases at issue here are still outside that class.

The Circuit Court correctly determined Trustee Bob Bormann and Lorin Schmidt were not related and thus, no self-dealing occurred. This Court should affirm.

B. The terms of the leases with the Trust's tenants do not constitute self-dealing or any breach of fiduciary duty.

Petitioners alternatively contend the lease terms between Schmidt and the Trust demonstrate self-dealing and constituted a breach of fiduciary duty. Again, this Court reviews the Circuit Court's conclusion under the clearly erroneous standard. Abundant evidence supports the Circuit Court's determination that no breach of fiduciary duty occurred. The rental values for all the property were reasonable and appropriate. This Court should affirm the Circuit Court.

Petitioners mistakenly assert Trustees are automatically "liable" if the Trust land was not rented for a certain amount. A trustee's duty is not measured merely by whether he blindly rented trust property for the highest possible value. The RESTATEMENT (SECOND) OF TRUSTS directs trustees to consider a variety of factors when leasing trust property:

> A trustee having power to make leases can properly make only such leases as under all the circumstances are reasonable. In determining whether a lease is reasonable the following circumstances among others are considered: (1) the purposes of the trust; (2) the probable duration of the trust; (3) the nature and extent of the interests of the beneficiaries; (4) the value of the property; (5) the nature of the property and the uses to which it may be advantageously put; (6) other powers which the trustee has with respect to the property; (7) the usual and customary methods of dealing with such property in the locality in which it is situated; (8) the conditions existing at the time of the lease.

RESTATEMENT (SECOND) OF TRUSTS § 189 cmt. b (1959).

After two of the beneficiaries demanded the Trustees convert the leases to cash rent to try and stabilize income, Trustees undertook an in-depth analysis of historic crop

yields and other metrics to arrive at cash rental rates for the different parcels of land beginning in 2007. (App. 36, p. 37-38.) Trustees testified in detail how they arrived at the cash rental rates for all the parcels of land, including those rented by Schmidt. They used these same factors to arrive at cash-rent values each year since moving to cash-rent leases. (App. 40, p. 53.) First, the location of the Trust's land in western Hutchinson County and eastern Douglas County historically means lower rental rates than land in eastern Hutchinson County because it is less fertile and receives less rainfall. (App. 35, p. 34-35.) Trustees also considered rental rates in the immediate vicinity of the Trust parcels, soil quality, topography, drainage issues, and USDA documentation regarding rental rates for prior years in the two counties. (App. 35-37, p. 35-36, 40-41.) Moreover, Trustees used their experience of living in the area most of their lives, Bob's four decades of experience in agricultural lending and their experience with the parcels themselves, having inspected them on numerous occasions. (App. 35, p. 36.) Trustees also take into consideration the Trust's probable duration. They recognize multi-year leases are impossible because the income beneficiaries are elderly and the Trust property must be sold when Joseph's last niece or nephew dies. (App. 38, p. 46-47.) Finally, Trustees evaluated the four most recent years of production history for the parcels from 2003 through 2006. (App. 35-36, p. 36-37; HE 104.)

That analysis revealed that Schmidt's production from his two parcels was less than the remaining parcels by roughly 20 percent.

OTHER RENTERS:

	Douglas County	Hutchinson County	2003-2006 Average
Corn	113.12	97.88	105.50

Beans	36.38	32.56	34.47

LORIN SCHMIDT

	Douglas County	Hutchinson County	2003-2006 Average	Percentage Difference
Corn	72.38	94.37	83.37	-20.97%
Beans	31.24	36.42	33.83	-1.86%

(HE 104; App. 36, p. 39.)

Schmidt's lone parcel in Douglas County was also compared to DuWayne Bialas's parcel in that county during that timeframe. Schmidt's parcel produced thirty percent less than Bialas's.

DUWAYNE BIALAS

	2006	2005	2004	2003	Avg. Yield
Corn	63.54	96.55	149.32	143.05	113.12
Beans	42.91	27.09	41.87	33.64	36.38

LORIN SCHMDIT

	2006	2005	2004	2003	Avg. Yield	Percentage Difference
Corn	24.09	82.06	82.87	100.50	72.38	-36.01%
Beans	40.40	22.40	30.40	31.74	31.74	-14.14%

(HE 104; App. 36, p. 39.) In fact, Schmidt's parcel in Douglas County is the poorest producing property owned by the Trust. (App. 36, p. 39.)

Bob explained why Schmidt's property in Douglas County produced less, even though its soil quality rating may be similar to other parcels. The southern portion of that parcel is landlocked and very low while the northern portion has a higher elevation. (*Id.*) That means that when the area receives significant rainfall or snow, water accumulates in the southern portion of the property and its poor drainage causes standing water, leading

to reduced yields. (*Id.*, p. 39-40.)

In addition, Trustees also looked to the USDA county-specific cash rental survey as a guide. (App. 37, p. 42.) However, the charts have limitations based upon number of respondents and the differences in land quality even in the same county. (*Id.*) Indeed, the James River means the production is different in the two sides of Hutchinson County. (App. 59, p. 131-32.) Still, the rental rates established by Trustees are well within the USDA's range of average rental rates in both Douglas and Hutchinson County, taken together with the production records and other factors evaluated by Trustees. (*See* HE 111.)

Notably, four years of actual production history, like that used by Trustees to set the cash rental rates, is also used by the federal government to establish federally-subsidized crop insurance programs. *See, e.g.*, William Edward, *Actual Production History and Insurance Unites for Multiple Peril Crop Insurance*, http://www.agrisk.umn.edu/cache/ARL02120.pdf (last visited February 6, 2015) (first step in crop insurance is to establish "Actual Production History", which requires yields for a minimum of four consecutive years).

The Circuit Court determined the evidence did not support Petitioners claims that Schmidt received a "sweetheart deal," and that the productivity records and other factors Trustees considered fully supported the rental rates charged. Rather than focusing on the comprehensive list of factors used by Trustees and adopted by the Circuit Court, Petitioners attempted to cherry-pick a few data points they claimed supported their position.

First, Petitioners argued the soil quality ratings should determine the cash rental

values. However, soil quality rating alone does not reflect proper rental rates for land. Even if two pieces of property have the exact same soil type, they may not produce the same crop because of other factors, including farming practices, topography, drainage, and rainfall. (App. 59, p. 131.)

Second, Petitioners' proposed rental rates were based on an SDSU agricultural land market survey averaging the rental rates for Bon Homme, Hutchinson, and Yankton Counties, rather than Hutchinson County and Douglas County alone. (App. 72, p. 182.) As the Circuit Court recognized, using three counties skews that average. (App. 80, p. 216.) For example, the USDA average rental rate for Hutchinson County in 2012 was $106, while the SDSU survey's average rental rate was $152.50 when Bon Homme and Yankton Counties were included. (*Compare* HE 102 *with* HE 114.)

Gene Loos was Petitioners' only witness on rental rates. He freely admitted the shortcomings in the SDSU survey and that he did very little to independently investigate rental rates. (App. 72-73, p. 184-88.) Further, Gene Loos is an owner of a commercial insurance business in Sioux Falls and owns no property in either Hutchinson or Douglas Counties. (App. 73, p. 185.) Thus, he was poorly qualified to testify on appropriate rental rates.

In its findings of fact, the Circuit Court methodically rejected all of Petitioners' challenges to the rental rates:

> So what do we have? We have an allegation that it was rented because of a family relationship. There is the presentation of figures that would attempt to show that there is a beneficial rental rate that was applied to that familial relationship, if you wish to characterize it that way.
>
> But the court does not find that to be true. The court, based upon the evidence, finds that the determination as to the value of the rental was calculated based upon the production in the years prior to the change.

> The change from crop sharing to cash rent was at the request of the beneficiaries. They wanted stability. The evidence also shows that there is a great disparity between the amount of income in one year as opposed to another. The court makes note that if you cherry-pick figures [as Petitioners did at hearing and in their appeal brief], you are going to come up with the ability to state in any one particular instance that it is under-rented as far as the rate, and another time you can say it's over-rented as to a rate.
>
> The court – in looking at the figures that have been submitted in the exhibits showing rental across territories, the court makes note that it is a very difficult calculation to come up with an amount that is the amount that is a disparity so that we can determine that the trustees failed to carry out their duties to the beneficiaries. The court has examined the figures, and the court finds that the amount calculated by Mr. Loos is not supportable. If you take the high values on everything, you are not going to be able to calculate a valid rental amount.
>
> . . .
>
> Now, if we were only looking at providing the maximum possible income to the beneficiaries, which I'm sure is what they would like, then you would go out, advertise it, but in most instances, as detailed in argument, they would want for a longer time period. They are not someone who wants one year and then another year.
>
> And because of the structure of this trust and the fact that the termination of the trust could happen at any time, because it is totally dependent upon the lives that are present currently, and when their date of death may happen, . . . it could terminate tomorrow. So you cannot rent for long periods of time.
>
> The submissions that have been provided by the parties have been submissions from documents submitted technically by both sides. There has been no expert who was retained and brought in who said that the amount for the rent was a value that was so at variance with the true rental value that the court can find that it would be in violation of the fiduciary duties of the trustees.
>
> The court makes note that there are and is no finding by this court that there is a violation of the trust responsibilities and the fiduciary responsibilities of the trustees.

(App. 80-81, p. 215-18.) (emphasis added).

Simply put, abundant evidence supports the Circuit Court's conclusions that no

breach of fiduciary duty occurred due to the Trust's leases with Schmidt. Schmidt did not receive a better deal than anyone else renting land, but paid a reasonable price based upon a number of appropriate factors.

In practice, Trustees complied with their duties by renting the land as Joseph did during his lifetime and intended after his death. In doing so they recognized and accommodated the careful balance between the current income beneficiaries and the contingent remaindermen in accordance with the criteria in RESTATEMENT (SECOND) OF TRUSTS § 189 cmt. b (1959). The Circuit Court correctly recognized Trustees properly struck this balance due to the purposes and probable duration of the Trust. Petitioners completely failed to establish a breach of duty by Trustees – let alone a "willful default" under the Trust Instrument.

3. The Circuit Court correctly determined Trustees did not breach any fiduciary duties and nothing warranted Trustees' removal.

At hearing, Petitioners alleged a number of breaches of duty by Trustees. The Circuit Court, after hearing all the evidence and judging the credibility of the witnesses, rejected Petitioners' arguments on every front. Trustees committed no breach of fiduciary duty and did nothing to justify the drastic remedy of removal.

Petitioners claim the removal of a trustee is a legal question reviewed *de novo*. As noted previously, the applicable standard of review is actually the abuse of discretion standard. *Estate of Unke*, 1998 S.D. 94, ¶¶ 26 & 29, 583 N.W.2d 145, 150 n. 4. Petitioners also ask the Court to apply a *de novo* review regarding the Circuit Court's decision finding no breach of duty by Trustees. This is contrary to this Court's prior determinations that the question of whether a trustee has breached any duty is reviewed under the clearly erroneous standard. *In re Estate of Moncur*, 2012 S.D. 17, ¶ 10, 812

N.W.2d 485, 487 (citations omitted). The Circuit Court properly determined Trustees did not breach any fiduciary duties and should not be removed. This Court should affirm the Circuit Court.

A. Removal of a Settlor's hand-picked trustee is a drastic action.

The removal of a trustee is a drastic action that should not be undertaken absent clear necessity. *See, e.g.*, *In re Trust made by Giles*, 74 A.D.3d 1499, 1503 (N.Y. App. Div. 2010) (citation omitted). For purposes of this case, it is imperative to remember Joseph specifically named Paul and Bob as trustees in the Trust Instrument:

> When the settlor of a trust has named a trustee, fully aware of possible conflicts inherent in his appointment, only rarely will the court remove the trustee, and it will never remove her for a potential conflict of interest but only for demonstrated abuse of power detrimental to the trust.

In re Betty A. Luhrs Trust, 443 N.W.2d 646, 651 (S.D. 1989) (citations omitted).

Moreover, "[w]ithout a demonstration that the trust corpus is in danger of dissipation, mere displeasure of a beneficiary is an insufficient reason for removing a testamentary trustee." *Id.* (citations omitted). *See also Schildberg v. Schildberg*, 461 N.W.2d 186, 191 (Iowa 1990) (court will not ordinarily remove a trustee appointed by the settlor); *In re White*, 484 A.2d 763, 765 (Pa. 1984) ("[W]here a settlor appoints a particular trustee, removal should only occur when required to protect the trust property."); *Matter of Amason's Estate*, 369 So. 2d 786, 790 (Ala. 1979) ("The removal of a trustee is such a drastic action that it should be taken only when the estate is actually endangered and intervention is necessary to save trust property.").

Here, Joseph specifically asked Paul and Bob to act as trustees. Had Joseph wanted his land managed by some other person or entity, he would have set the Trust up that way. He did not. Neither Bob nor Paul act as trustees because they need the money.

(App. 60, p. 135.) They do so because they promised Joseph they would. (*Id.*) "The court's task is to ensure that the intentions and wishes of the settlor are honored." *Luke v. Stevenson*, 2005 S.D. 51, ¶ 8, 696 N.W.2d 553, 557 (citation omitted). The Circuit Court's rulings accomplished that ultimate goal.

B. Trustees breached no fiduciary duties and removal is not proper.

Petitioners sought removal of Trustees premised on the erroneous assumption that the Trustees breached their fiduciary duties. As explained below, Petitioners failed to establish any breach.

i. No conflict of interest or self-dealing occurred.

First, Petitioners continue to allege Trustees' failure to disclose the "relationship" between Bob and Schmidt constituted a breach of trust. As explained above, no self-dealing occurred as Bob and Schmidt are not related.

ii. Trustees provided information when Loos requested it.

Petitioners also claim Trustees violated SDCL § 55-2-13 by not providing information to Gene Loos. The crux of Petitioners' argument is that the Trustees "resisted" providing Loos with information regarding the cash rent leases "for a year" and "only provided that information after Petitioners had begun this litigation and sent formal discovery requests for the leases." (Petitioner's Brief at 30-31.) The actual record belies this claim.

Gene Loos first contacted Michael Braley, counsel for the Trustees, in early January 2013, to ask how many total acres the Trust owned. (Petitioners' Brief at 12-13.) During cross examination, however, Loos twice admitted that *he knew* how many acres the Trust owned before making the request because he had visited every parcel owned by the Trust several times in the last three to four years. (App. 73-74, p. 188, 190.) In any

event, Braley responded to Loos's inquiry and told him the Trust owned approximately 900 acres. (App. 65, p. 153.) Petitioners then claim Loos sought copies of the Trust's lease agreements in an email dated January 19, 2013, and that he wanted the rental rates for each parcel of land. (Petitioner's Brief at 13.) However, when asked specifically to point out in his communications with the Trustees or Braley where he asked for copies of the lease agreements, Loos admitted he never did this. (App. 74, p. 189.) He admitted he was only looking for the location of the parcels, but then admitted a second time he already knew where each parcel was located prior to making the inquiry. (*Id.*, p. 189-90.)

Even so, Bob contacted Loos directly in January, 2013, to discuss his inquiries. Petitioners acknowledge Bob told Loos rents were not raised in 2013 due to the severe drought the year prior. (Petitioners' Brief at 13-14.) They claim, however, that Bob did not "disclose" the rental rates for each parcel. (*Id.*) Notably, however, Petitioners do not say Bob was actually asked for the rental rate for each parcel during the phone call. Indeed, Bob answered all the questions Loos had. If any concern existed, Loos did not make it known as he did not appear at the hearing for the 2012 accounting, despite knowing when it would be held, and did not contact the Trustees again until August 28, 2013. (HE 15; App. 74, p. 189.)

In August, 2013, Loos requested a meeting with Trustees to discuss rental rates for the Trust land. (HE 15.) Bob called Loos and told him what was transpiring with the leases. (*Id.*) Loos sent an email thanking Bob for the phone call and for providing him the information he sought concerning the Trust property. (*Id.*; App. 74, p. 190-91.) He then asked Bob if he was available to meet. (HE 15.) Bob told Loos he was willing to meet with him at a future date. (*Id.*; App. 74, p. 191.)

Rather than take Bob up on this offer, however, the very next communication Trustees received from Loos was a letter from the Woods Fuller Law Firm five days later demanding their resignations in exchange for a release of all claims. (HE 15; App. 74, p. 191-92.) Notably, Petitioners offered this full and complete release despite their present complaints that the rental rates were too low and significantly damaged the Trust. Put simply, Gene Loos's only real goal was to bully Trustees into resigning so he could control the Trust against Joseph's wishes. Both the Trustees and the Circuit Court appropriately rebuffed those efforts.

iii. Other alleged breaches of trust.

Petitioners also assert other alleged breaches of trust allegedly justifying Trustees' removal. These allegations can be fairly described as nitpicking. Moreover, Petitioners cite no law that justifies removal based upon isolated, inconsequential mistakes by a trustee over decades of service. This Court should affirm the Circuit Court.

First, Petitioners claim the inadvertent placement of 14 pages of unrelated documents into the Trust file constitutes a breach of trust. The documents date from 2003 through 2008. (HE 14.) The Trust file, in the Circuit Court's own words, "is voluminous." (App. 79, p. 211.) The Circuit Court, after hearing Petitioners' argument regarding the misfiling of these pages, properly determined it was not a breach of trust. (App. 81, p. 219-20.) Put simply, misplacing 14 pages into a file spanning thousands of pages hardly amounts to a breach of trust.

Second, Petitioners claim Trustees missed two payments over 35 years causing the Trust to incur late payment charges. The Circuit Court rejected this as a breach of trust. Petitioners spent countless hours scouring thousands of documents in the Trust file for errors and located a tax penalty of $27 in 2009 and a finance charge of $36.38 in

2005, a total of $63.38 in all the years of Trustees' service. (App. 47-48, p. 83-85.) Bob explained that Trustees did not forget to pay the tax bill but that the bill payment flipped out of the automated postage machine and fell behind a counter. (App. 48, p. 85.) Even so, the Circuit Court noted that this was not an onerous amount, did not warrant finding a breach of trust, or support removal.

Third, Petitioners briefly contend Trustees have breached trust by only leasing Trust property to customers of Farmers State Bank. During his lifetime, Joseph rented his farmland to customers of Farmers State Bank and was himself, a customer of the bank. (App. 33, p. 25; HE 103.) If Joseph saw a conflict with regard to his land being rented to the bank's customers after he died, he could have made that clear. *See Schildberg*, 461 N.W.2d at 191 (citations omitted) ("the court will not ordinarily remove a trustee appointed by the settlor for grounds existing at the time of the trust's creation and known to the settlor"). Instead, he wanted the Bialases to continue renting the land as long as they wanted and wanted other good stewards to rent his property. He trusted the Bormanns. Moreover, until approximately 1999, Farmers State Bank was the only bank in Parkston. (App. 35, p. 34.) If Trustees did not rent to customers of the bank, the number of potential tenants would be drastically reduced, which could adversely affect the Trust. This does not constitute a breach of trust.

Fourth, Petitioners claim Trustees indirectly benefitted themselves by keeping a small cash reserve at Farmers State Bank. Again, Joseph trusted Vern Bormann so much that he specifically named him as an initial trustee. (App. 21, p. 21.) If Joseph's handpicked Trustees' decision to keep a small cash reserve in the bank Joseph himself used amounts to a breach of trust, then, Petitioners are in essence, asserting that Joseph

breached the trust by appointing Vern and his sons as successors. After all, he could have directed where the Trust funds be kept. The Circuit Court correctly rejected this as a breach of trust.

Fifth, Petitioners claim Braley referenced documents in proposed orders that allegedly were not served on any party and were not filed with the Court when the proposed order was submitted, constituting a breach of trust. This is a red herring. Braley drafted proposed orders and sent them to the Circuit Court for review with the annual accounting. The proposed order would state that the Circuit Court had reviewed a "voucher" containing documents supporting the accounting, including tax assessments and tax records for payment of real estate taxes, for example. (App. 66, p. 157.) According to Petitioners, these documents were not filed with the Court at that time. However, if a person wanted to inspect the Trust file to determine how much land the Trust owned, the vouchers for every prior year would be present, showing exactly what the Trust owned. Additionally, the Circuit Court stated it was aware of issues with the clerk's office receiving items but not filing them even though they had been received. (App. 81, p. 220.) Therefore, the file-stamped date on the "voucher" may have differed from the date the documents may have been filed. (*Id.*) The Court ruled the placement of "vouchers" in the file was not problematic, that the Court had reviewed the "vouchers" and the accountings, and that they were proper. (App. 81-82, p. 220-21.)

Further, no statute requires Trustees to serve all the documents supporting an annual accounting on the beneficiaries. Rather, Trustees need only serve a summary accounting. SDCL § 21-22-30. Petitioners argue Trustees needed to also include copies of the leases, names of tenants, all relationships between tenants and Trustees, and rents

per acre. The Circuit Court properly rejected this argument on the renewed motions for summary judgment and again after the evidentiary hearing on the 2013 Accounting. Put simply, there is no such onerous requirement in SDCL § 21-22-30. Petitioners' interpretation of the statute would greatly expand the duties of trustees and represents a significant change in how routine annual accountings are handled in this State.

This Court's decision in *In re Guardianship of Larson*, 1998 S.D. 51, 579 N.W.2d 24, provides guidance. There, this Court rejected beneficiaries' challenge "to methods of reporting they had previously acquiesced to" in the guardian's annual accounting filed with the court. *Id*. at ¶ 5, 579 N.W.2d at 25. *Larson*, therefore, reflects the rule that a beneficiary cannot acquiesce in a certain reporting method for years only to suddenly challenge it. Here, that principle bars Petitioners from claiming the accountings were insufficiently detailed.

Additionally, *Larson* held that a grand total listing the expenses was sufficient and rejected claims that the accounting was required to list each individual transaction. *Id.* at ¶ 18, 579 N.W.2d at 28 ("the trial court was not 'clearly erroneous' in its determination that the $36,905 reported as cash expenditures for Harold's benefit is somehow inadequate reporting."); *See also Zuch v. Conn. Bank & Trust Co*., 500 A.2d 565, 568 (Conn. Ct. App. 1985) ("The trial court erred when it ruled that the scope of the accounting due the plaintiff should include a justification by [the trustee] of its investment policies during its management of the trust, the projected rate of earnings for each year and an evaluation of the propriety of the investments made by the [the trustee]."). Accordingly, Trustees' accountings were sufficient and do not constitute a breach of trust.

Sixth, Petitioners claim Braley's clerical error resulting in two legal descriptions of Trust land being left off past accountings constitutes a breach of trust that requires removing Trustees. At the evidentiary hearing, though, Petitioners' only witness twice admitted he knew how many acres the Trust owned. (App. 73-74, p. 188, 190.) There is no evidence suggesting that Braley's clerical error misled Petitioners regarding how many acres the Trust owned.

Seventh, Petitioners claim Trustees only purchased liability insurance for 680 acres of the Trust property. This was obviously also based on Mr. Braley's clerical error. The Court rejected this as a breach of trust, stating that the value of the liability insurance would still cover the land. (App. 81, p. 220.)

Finally, Petitioners contend that Trustees did not serve the contingent remaindermen with the annual accountings, requiring their removal. However, no contingent remainderman, other than Gene Loos, sought to reopen the accountings or joined in the objections to the 2013 accounting despite knowledge of the objections. Indeed, the contingent remaindermen have no actual interest in the outcome of Petitioners' challenge because they have no right to Trust income. *See In re Estate of Wallbaum*, 2012 S.D. 18, ¶ 41, 813 N.W.2d 111, 121 ("because Florence's grandchildren had no interest in the income First Dakota distributed to Douglas, they did not suffer any 'actual or threatened injury' as a result of First Dakota's actions. Florence's grandchildren thus do not have standing to assert a claim against First Dakota for its failure to make quarterly income distributions to Douglas."). *See also In re Will of Frye*, 2009 WL 250355, at *3-4 (Iowa Ct. App. 2009) (remainder beneficiary who claimed the trustee did not obtain a high enough rental value for trust property lacked standing to

challenge the acts of the trustee because the beneficiary had no current right to receive income). Accordingly, service on the contingent remaindermen was unnecessary and certainly did not amount to a breach of trust warranting the drastic remedy of removal.

The Circuit Court, after hearing all the evidence on these matters, rejected Petitioners' arguments on every front. Trustees have committed no breaches of duty and nothing warrants removal. This Court should affirm the Circuit Court.

4. The Circuit Court properly granted summary judgment to Trustees regarding Petitioners' claims to reopen the 2009 through 2012 accountings.

Finally, Petitioners claim the Circuit Court erred when it granted summary judgment to Trustees regarding Petitioners' request to reopen the 2009 through 2012 Court-approved accountings. They claim Braley's clerical error in omitting two legal descriptions was a material omission requiring the accountings to be reopened. This argument lacks merit. The Circuit Court, after reviewing the 2009 through 2012 accountings, Braley's affidavit, and the materials available in the record, properly granted summary judgment to Trustees.

SDCL § 21-22-30 bars any claims arising out of a trustee's accounting of a Court-supervised trust after the accounting is approved by the court. It provides:

> An accounting by a trustee of a court supervised trust and the final approval thereof by a court is conclusive against all persons in any way interested in the trust, and the trustee, absent fraud, intentional misrepresentation, or material omission, shall be released and discharged from any and all liability as to all matters set forth in the accounting. For purposes of this section, the term, accounting, means any annual, interim, or final report or other statement provided by a trustee reflecting all transactions, receipts, and disbursements during the reporting period and a list of assets as of the end of the period covered by the report of statement.

SDCL § 21-22-30.

In April 2014, the Circuit Court held a hearing on Trustees' Motion for Summary

Judgment on the Petition to Reopen the 2009 through 2012 accountings. At the hearing, the Court determined accountings for 2009 through 2012 were missing legal descriptions for two of the nine parcels owned by the Trust. (App. 2-3, p. 2-3.) The Court stated the missing legal descriptions needed to be addressed before the Court would grant Trustees' Motion for Summary Judgment. (App. 5-6, p. 5-6.)

Trustees submitted an affidavit from Braley explaining that the omission of the legal descriptions was not intentional but the result of a mere word-processing error. (R 915-20.) The accountings were filed that way and approved by the Court for 19 years without anyone noticing the missing legal descriptions. (*Id.*) All accountings prior to that had been filed with all the legal descriptions. Even so, the Court file showed all parcels remained in the Trust and included annual tax assessments, tax payment receipts, and other documents referencing all the parcels. (*Id.*)

More fundamentally, Petitioners never claimed the unintentional omission of the legal descriptions for the two parcels formed the basis for their original Petition. In fact, the Petition makes no mention at all of omitted descriptions. (R 595-613.) Rather, it claims the accounting should be reopened due to fraud and self-dealing, although, at the first summary judgment hearing, Petitioners' counsel backtracked from the fraud allegations. (App. 4-5, p. 4-5.)

For the omission of the legal description of the parcels to be material, (1) the omission would have to be unknown to Petitioners and (2) Petitioners' claims would need to be based on the omission. *See* Black's Law Dictionary (9th ed. 2009) (defining "material" as "of such a nature that knowledge of the item would affect a person's decision-making; significant; essential"). Petitioners make no effort to bridge this gap.

Petitioners each submitted an affidavit to the Court in opposition to Trustees' Motion for Summary Judgment. They could have included a sentence attesting that they always thought the Trust only owned 680 acres of land instead of 920 acres. Obviously, no beneficiary was willing to make that assertion under penalty of perjury. Moreover, Gene Loos filed a carefully crafted affidavit in response to Trustees' renewed motion and had the opportunity to claim he was misled or that his claims were based upon the omission of the legal descriptions of the parcels. He did not. Put simply, the total amount of acres owned by the Trust was not unknown to Petitioners and their claims were never based upon the omission.

As a practical matter, the Circuit Court's summary judgment order remained interlocutory until after the September 12, 2014, evidentiary hearing on the 2013 Accounting Petition. The Circuit Court could have reversed itself at any time on the summary judgment decisions. The evidence Petitioners put on during the September 12, 2014, hearing is exactly the evidence they would have put on if the Circuit Court had denied Trustees' motion for summary judgment and reopened the accountings. In effect, Petitioners received the benefit of putting on all their evidence to reopen the 2009 through 2012 accountings when they challenged the 2013 Accounting. Importantly, they offered no supportable evidence at that time that they did not know how many acres the Trust owned. Indeed, Loos admitted knowing for years' prior how many acres the Trust owned. (App. 73, p. 188.) Accordingly, Petitioners' effort to blow this clerical error out of proportion fails.

In short, our Legislature recognizes that trusts are an integral part of South Dakota's economy. Trustees in this State rely upon Court-approved accountings and

SDCL § 21-22-30 to ensure that trusts can be effectively managed for the benefit of the beneficiaries with finality offered by court approval of past accountings. Reopening a prior Court-approved accounting is a grave endeavor that the Legislature has prohibited absent a showing of fraud, intentional misrepresentation, or material omission, of which Petitioners have no proof. Indeed, the only claim they advance is based on a clerical error, but that is hardly material given that they admittedly knew how much land the Trust owned and exactly where it was located. The Circuit Court's grant of summary judgment to Trustees should be affirmed.

5. Petitioners are not entitled to damages.

The Circuit Court correctly determined the Trustees fulfilled their duties. Therefore, Petitioners are not entitled to damages as requested in their brief. Moreover, Petitioners have certainly not identified any "willful" breach as required under the Trust Instrument to support an award of damages.

Given the history reflected in the record, Petitioners' damages claim rings especially hollow. Again, Loos offered a full release if Trustees would just resign so he could control the Trust. Presumably, if Loos actually thought his aunts, uncles, and mother had been so seriously damaged, he would not have so quickly offered to waive any damages claim. Here again, this shows the real goal has always been to force Trustees out against Joseph's express intent. Petitioners are not entitled to damages and provided no evidence to that effect.

CONCLUSION

This Court should affirm the Circuit Court on all issues.

Dated at Sioux Falls, South Dakota, this 2nd day of March, 2015.

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CERTIFICATE OF COMPLIANCE

The undersigned hereby certifies that this Brief of Appellees complies with the type volume limitations set forth in SDCL § 15-26A-66. Based on the information provided by Microsoft Word 2010, this Brief contains 9,067 words and 46,772 characters, excluding the table of contents, table of authorities, jurisdictional statement, statement of legal issues, any addendum materials, and any certificates of counsel. This Brief is typeset in Times New Roman (12 point) and was prepared using Microsoft Word 2010.

Dated at Sioux Falls, South Dakota, this 2nd day of March, 2015.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing "Brief of Appellees" was filed electronically with the South Dakota Supreme Court and that the original and two copies of the same were filed by mailing the same to 500 East Capital Avenue, Pierre, South Dakota, 57501-5070, on March 2, 2015.

The undersigned further certifies that an electronic copy of "Brief of Appellees" was emailed to the attorneys set forth below, on March 2, 2015:

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IN THE SUPREME COURT
OF THE
STATE OF SOUTH DAKOTA

No. 27273

GLORIA LOOS, LOUIS HOHN,
EVELYN LANG, VIRGINIA BINDER,
AND GENE LOOS,

Appellants,

v.

ROBERT AND PAUL BORMANN,

Appellees.

Appeal from the Circuit Court
First Judicial Circuit
Hutchinson County, South Dakota

HONORABLE GLEN ENG
HONORABLE PATRICK SMITH

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Notice of Appeal filed November 26, 2014

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ARGUMENT

This case requires that the Court examine the most basic, yet fundamental duty a trustee owes to a beneficiary, i.e. the duty of loyalty and good faith. It is curious that the trustees characterize this case as Gene Loos's attempt to wrestle control of the Baumgart trust from the trustees, when the petitioners have always requested that a third-party, corporate trustee replace the current individual trustees. The Court's analysis of the duty of loyalty in this case has far reaching implications for South Dakota's status as a favored trust jurisdiction. Nothing is more important in the trust industry than upholding a trustee's duty of loyalty and good faith.

Even more, the trust Grantors who choose South Dakota as their trust jurisdiction and rely on its courts to supervise their trustees, must have certainty that the supervising court will exercise supervision and independent judgment, and not merely rubber stamp trustee accounts.

1. Disposition of this case begins, and ends, with the duty of loyalty.

The trustees argue the Schmidt lease is valid because Robert Bormann and Lorin Schmidt are not related by blood or affinity and the Schmidt rental rate was fair. The trustee's arguments are not supported by law or fact.

A. The trust leases breach the duty of loyalty.

While SDCL § 55-4-13 does provide a specific list of persons with whom a

trustee may not deal, the statute is not exclusive. SDCL § 55-4-13 does not erode hundreds of years of common law and SDCL § 55-2-1 (South Dakota's duty of loyalty codified), which define self-dealing as any transaction that may place a trustee's personal interest ahead of that of a beneficiary or where a beneficiary or third party may question whether a trustee's action is in the beneficiary's best interest. *In re Estate of Stevenson*, 2000 S.D. 24, ¶¶ 9-11, 605 N.W.2d 818, 821.

> Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate.

Meinhard v. Salmon, 249 N.Y. 458, 464 (N.Y. 1928). Three rationales for strict construction of the duty of loyalty are apparent in this case.

> [Firstly] it is difficult, if not impossible for a person to act impartially in a matter in which he has an interest.
>
> . . . .
>
> Secondly, the courts have realized that fiduciary relationships lend themselves to exploitation. . . . [T]he success of the trust relationship will depend on the ability of the beneficiary to trust the trustee. . . . The only way to insure that the beneficiary can sleep at night in free and easy reliance on the loyalty of the trustee is to remove all serious temptations to disloyalty.
>
> . . . .
>
> Finally, . . . disloyal conduct is hard to detect. . . . [A] court, inquiring into [trust] administration at a later date, cannot expect to match the trustee's knowledge. . . . A wide variety of determinations can generally be supported by plausible argument, and rationalizations made after the fact will generally be unassailable.

Hallgring, *The Uniform Trustees' Powers Act and the Basic Principles of Fiduciary Responsibility,* 41 Wash. L. Rev. 801, 808-11 (1966).

The basic facts in this case, which demonstrate a violation of the trustees' duty of loyalty, are undisputed. First, SDCL § 55-4-13 specifically prohibits the trustees from leasing property to business associates. While "business associate" is not defined in South Dakota's code, a lender-borrower relationship surely fits. Each tenant of the trust, including Lorin Schmidt, is a customer of the trustees' bank.

Second, the Court in *Stevenson* did not once discuss SDCL § 55-4-13, blood relations, or affinity relations when it invalidated a lease among a trustee and a trustee's husband's cousin. Rather, the Court focused on a breach of the trustees' duty of loyalty. 2000 S.D. 24, ¶¶ 9-17, 605 N.W.2d 818, 821-23. The duty of loyalty does not end at a bloodline. Rather, when "it is shown that the trustee in making [a lease] was improperly influenced by his relationship to the [tenant] or even his friendship for the [tenant], so that he [leased] the property for less than he could have obtained from others . . . he commits a breach of trust." RESTATEMENT (SECOND) OF TRUSTS § 170, *comment e.*

Robert Bormann's grandson is Lorin Schmidt's grandson. When their common grandson was a couple of years old and at the time of their children's marriage to each other, the trustees terminated a long time tenant's lease and began

a lease relationship with Lorin Schmidt. When trust leases were converted to cash leases, Lorin Schmidt always received, and continues to receive, a preferential rental rate. The lease among grandpas at a discounted rate surely causes the beneficiaries to question whether the trustee has divided his loyalty in the transaction. In addition, Robert Bormann's assertion at trial that he has a duty to tenants demonstrates his loyalties are divided. (App. 57-58 "Q. Okay. And what do you understand your duty to be as trustee? A. I understand the duty as trustee in this trust to be one of fairness, one of good husbandry of the property, and one to be as accurate as I can be. Q. Fairness to whom? A. All parties. Q. So you believe you have a duty to the tenants . . . A. Yes.") The lease to Schmidt is a breach of the duty of loyalty.

B. Schmidt's rental rate breaches the duty of loyalty.

The Trustees want the Court to focus on Schmidt's land as it compares to the average statistics for all other land owned by the trust and rented to members of the Bialas family. The other land, however, was not encumbered by a single lease, but four leases. When comparing each trust parcel subject to a lease, the trustees' validation for a discount to Schmidt erodes. When the lump sum data the trustees purportedly relied on when setting rental rates is parceled out, it shows:

Crop	2003 (yield)	2004 (yield)	2005 (yield)	2006 (yield)	Average yield (03-06)	Tenant	Parcel
Corn	143.05	149.32	96.55	63.54	113.12	DuWayne Bialas	36-100-62 (Douglas)
Corn	137.19	144.92	82.05	53.03	104.2975	Larry Bialas	20-100-61 (Hutchinson)
Corn	138.85	141.98	85.49	22.66	97.245	Kurt Bialas	8-99-61 (Hutchinson)
Corn	108.72	137.75	98.09	32.91	94.3675	**Lorin Schmidt**	19-99-61 (Hutchinson)
Corn	119.48	141.67	78.34	28.89	92.095	Craig Bialas	29-100-61; 33-100-61 (Hutchinson)
Corn	100.50	82.87	82.06	24.09	72.38	**Lorin Schmidt**	27-99-62 (Douglas)

(App. 263)

This table shows that the average corn yield difference between DuWayne Bialas and Craig Bialas was 20 bushels. They were charged the same rent. But a 20 bushel difference, on average, between Craig Bialas and Lorin Schmidt supposedly warranted a significant discount in rent.

Crop	2003 (yield)	2004 (yield)	2005 (yield)	2006 (yield)	Average yield (03-06)	Tenant	Parcel
Beans	34.26	48.47	27.16	39.46	37.3375	Larry Bialas	20-100-61 (Hutchinson)
Beans	35.65	42.71	26.07	41.25	36.42	**Lorin Schmidt**	19-99-61 (Hutchinson)
Beans	33.64	41.87	27.09	42.91	36.38	DuWayne Bialas	36-100-62 (Douglas)
Beans	31.74	30.40	22.40	40.40	31.24	**Lorin Schmidt**	27-99-62 (Douglas)
Beans	35.51	32.89	18.24	37.65	31.0725	Craig Bialas	29-100-61; 33-100-61 (Hutchinson)
Beans	27.77	33.7	17.09		26.18667	Kurt Bialas	8-99-61 (Hutchinson)

(App. 263)

This table shows an 11 bushel average yield difference in beans between Larry Bialas's land and Kurt Bialas's land. They were charged the same rent. In contrast, Lorin Schmidt's land was significantly discounted, even though his bean yields were some of the best. Other data also shows that Lorin Schmidt's land is not inferior to all of the Bialas land. As shown below, a difference in soil rating of over .7 resulted in the same rent for Craig and Larry Bialas. A difference of .05, however, between Lorin's worst rated ground and Larry's poorest ground resulted in a drastic discount to Lorin. Moreover, even though Lorin's Hutchinson County land rated .2 better than Larry's, Lorin's rent was at a significant discount.

Soil Rating	Tenant	Parcel
.874	Craig Bialas	29-100-61 (Hutchinson)
.865	Craig Bialas	33-100-61 (Hutchinson)
.853	Willard Bialas	8-99-61 (Hutchinson)
.837	Travis Bialas	36-100-62 (Douglas)
.821	**Lorin Schmidt**	19-99-61 (Hutchinson)
.808	Travis Bialas	36-100-62 (Douglas)
.801	Larry Bialas	20-100-61 (Hutchinson)
.796	**Lorin Schmidt**	27-99-62 (Douglas)

(App. 264)

The undisputed facts, when actually examined, do not support the circuit court's conclusion that Lorin Schmidt's discounted rent was warranted. Moreover, the trustees' admitted at trial that they had not looked at a single piece of objective crop yield data since 2006. Even if Bialases' lump sum averages versus Schmidt's

averages provided a valid reference for 2007, they certainly do nothing to help determine rent in 2009 and beyond. The trustees acknowledged production could vary year to year and in some years past, Lorin Schmidt's poorest rated land outperformed the Bialases's best land. Rather than reexamine the data, however, the trustees blindly continued Lorin Schmidt's preferential rental rate, which is a violation of the duty of loyalty.

2. The beneficiaries deserve a third-party, professional trustee.

Trustees named in a trust are not entitled to serve when they breach their duty of loyalty to the trust. The trustees attempt to isolate each breach to minimize the effect of each breach on the beneficiaries. They ignore, and hope the court will not notice, how the individual breaches worked together to hide the Schmidt discount. But it was the trustees' failure to disclose the relationship with Schmidt, failure to identify the number of acres owned by the trust on each accounting, failure to identify the various rental rates on each accounting, failure to deliver accountings to remainder beneficiaries, and failure to provide information to the beneficiaries when requested that allowed the Schmidt discount to go unchecked for so many years. Furthermore, when it came time for the 2012 accounting in 2013, the trustees did not even inform the supervising court that a beneficiary had questions regarding the trust administration. When the nondisclosure of questions regarding trust administration was raised during the summary judgment

proceedings, the trustees' lawyer even submitted a factually incorrect affidavit to the supervising court, which stated that no beneficiary had ever raised any question regarding the trust's administration. Each individual breach snowballed into a serious breach, which greatly impacted the beneficiaries' ability to protect their interests. Moreover, the supervising court, failed to exercise legislatively mandated supervision, which caused further harm to the beneficiaries.

In addition to the serious breach of trust caused by the Schmidt transactions, which warrant removal, the trustees should be removed for other specific breaches of South Dakota's trust code that the trustees characterize as nitpicking. The trustees argue that the Court should not be concerned when they deposit trust funds in a bank owned by them. SDCL § 55-2-2, however, specifically prohibits the practice. In fact, even a corporate trustee, under the common law, was prohibited from depositing trust funds in its own bank. RESTATEMENT (SECOND) OF TRUSTS § 170, *comment m*. While South Dakota's legislature has specifically authorized the practice for corporate trustees under SDCL § 55-4-11, the legislature has not authorized the practice for individual trustees. Maintaining the trust account at the Bormann's bank is prohibited by statute.

The trustees failed to provide to the beneficiaries information regarding the trust when reasonably requested in direct contravention of SDCL § 55-2-13. In *In re Green Charitable Trust*, 431 N.W.2d 491 (Mich. App. 1988), the court held that

trustees breached their duties to beneficiaries and removed the trustees, in part, because the trustees failed to keep the beneficiaries informed about transactions related to the trust's most valuable asset. *Id.* at 499-500. In this case, the trustees failed to disclose to the supervising court or the beneficiaries in their annual accountings the number of acres owned by the trust, the rental rate for each parcel owned by the trust, and the identity of and relationship with each tenant of the trust.

Like in *Green*, the trustees breached their duties to the beneficiaries by failing to keep the beneficiaries informed of transactions affecting the trust's real estate. This is not a technicality. The trust's real estate is the trust's only income producing asset. It is hardly unreasonable to expect a trustee to provide beneficiaries and a supervising court with basic information such as individual tenants and rental rates for a trust's most import asset.

The trustees rely on *In re Guardianship of Larson,* 1998 S.D. 51, 579 N.W.2d 24, for the proposition that a beneficiary cannot challenge a method of accounting that had been previously approved. The trustee's reliance on *Larson* is misplaced. *Larson* is a guardianship case, and the accountings were governed by the probate code, at that time SDCL Ch. 30-23 *Larson*, 1988 S.D. 51, ¶ 14, 579 N.W.2d at 27. The trustees' accountings, however, are governed by SDCL Ch. 21-22. The difference between a guardianship accounting and a court supervised trust

accounting is that guardianship accountings must be affirmatively challenged by interested persons at the time of the accounting, whereas a court supervised trust accounting need not be challenged by any beneficiary at any time because the supervising court is supposed to provide an independent review of all trust matters covered by the accounting. If a beneficiary later learns of a material omission within the accounting, the court supervised accounting is subject to challenge. SDCL § 21-22-30.

Section 21-22-30 recognizes that a court cannot perform its duty to review a trust accounting independently if there material omissions in the information provided to it, and that it would not be fair to the beneficiaries to preclude them from challenging an accounting with a material omission. The interested persons in *Larson* had reviewed the accountings and acquiesced in the form of accounting at each hearing. *Larson*, 1988 S.D. 51, ¶ 5, 579 N.W.2d at 25. In this case, the contingent remainder beneficiaries were not given copies of the accounting until 2013, and no hearing was held regarding accountings prior to 2013. Rather the supervising court approved the accountings as a matter of routine course, without any independent investigation into the trust transactions.

Where trustees continually and persistently breach their duty of loyalty to trust beneficiaries and for years the supervising court has left the trustees

unsupervised, beneficiaries of South Dakota trusts deserve to have the trustees removed and replaced by a third-party, professional trustee.

Conclusion

The importance of the duty of loyalty to South Dakota's trust economy and the Petitioners in this case cannot be overstated. Trustees must be held accountable for their actions and inactions. The trustees should be removed for their continual breaches of the duty of loyalty and the trust should be made whole for the damage caused by the trustees' actions.

Dated March 20, 2015.

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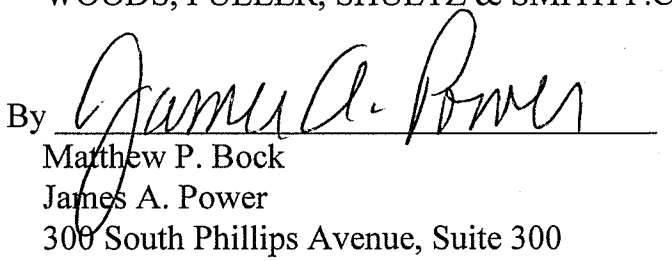
Certificate of Compliance

In accordance with SDCL § 15-26A-66(b)(4), I certify that this brief complies with the requirements set forth in the South Dakota Codified Laws. This brief was prepared using Word 2010, and contains 3,339 words excluding the table of contents, table of authorities, and certificate of compliance. I have relied on the word count of the word-processing program to prepare this certificate.

Dated this 20th day of March, 2015.

WOODS, FULLER, SHULTZ & SMITH P.C.

By 

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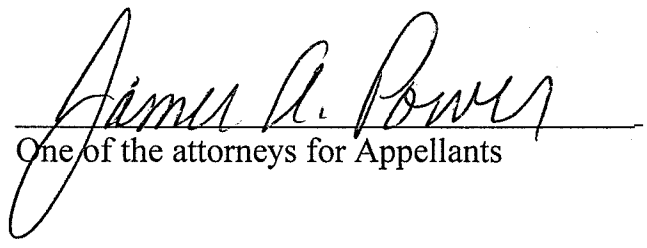

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