

NO. A06-1018

State of Minnesota
In Court of Appeals

In Re: The Naomi Margolis Revocable Trust

Barry Lorberbaum,

Appellant,

vs.

Jack Margolis,

Respondent.

APPELLANT'S BRIEF AND APPENDIX

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TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

STATEMENT OF THE LEGAL ISSUES..... 1

STATEMENT OF THE CASE..... 2

STATEMENT OF FACTS 3

STANDARD OF REVIEW 24

ARGUMENT 25

 I. The Trial Court Erred in Allowing Trustee Margolis’ Accounting, and In Approving His Request that the Trust Bear the Sole Burden to Pay the Nursing Home and Medical Expenses for Naomi Margolis 25

 A. The Trial Court Erred in Failing to Consider the Impact of Minn. Stat. §501B.14, Subd. 1(2) Which Disqualified Trustee Margolis from Making Distributions of Trust Assets for Nursing Home Expenses When Doing So Discharged His Legal Duty to Support His Spouse and Relieved His Personal Contractual Obligation To Pay Such Expenses 25

 1. The Language Of Section 2.2 Of The Trust Agreement Clearly Reflects The Intent Of The Grantor To Establish A Discretionary Power, Therefore, Section 2.2 Is Squarely Within The Domain Of Minn. Stat. §501B.14, Subd 1(2)..... 25

 2. Trustee Jack Margolis Clearly Owed A Duty Of Legal Support And Was Personally Liable For His Wife’s Medical Expenses 27

 3. The Trial Court Erred In Failing To Directly Consider The Impact Of Minn. Stat. §501B.14, Subd. 1(2) 28

 B. The Trial Court Erred When it Honored Jack Margolis’ Request to Allocate the Trust Income to Pay Naomi Margolis’ Nursing Home and Medical Expenses Before Any Other Assets in Which She had an Interest were Used, Because Jack Margolis is Not Entitled to Rely on Section 2.2 of the Trust Agreement Due to his Failure to Follow the Provisions of the Trust Agreement..... 30

 C. The Trial Court Erred When It Approved Jack Margolis’ Request to Allocate to the Trust the Entire Burden of Naomi Margolis’ Nursing Home and Medical Expenses Because his Request Was an Integral Part of a Course of Conduct

which Breached his Fiduciary Duty of Loyalty to the Trust Beneficiaries and was Motivated by an Improper Purpose 32

D. The Trial Court Erred When It Allowed Jack Margolis’ Request to Allocate the Use of Trust Income or Assets to the Nursing Home and Medical Expenses, Because Jack Margolis had Unclean Hands 34

II. The Trial Court Erred When It Held that Appellant Failed to Make a Sufficient Showing to Require the Trustee to Explain or Account for the Proceeds of the Norwest CD Listed in Naomi Margolis’ Notes in the Amount of \$100,000, and To Restore that Amount to the Trust..... 36

III. The Trial Court Erred When It Failed to Require Trustee Margolis to Make Restitution to the Trust 40

CONCLUSION..... 41

TABLE OF AUTHORITIES

State Cases

<u>Blythe v. Kujawa</u> , 175 Minn. 88, 220 N.W. 168 (1928)	36
<u>Burgeois v. Hurley</u> , 392 N.E.2d 1061 (1979)	1, 37, 38
<u>City of Minnetonka v. Carlson</u> , 298 N.W.2d 763, 766 (Minn. 1980).....	24
<u>Conway v. Emeny</u> , 139 Conn. 612, 96 A.2d 221 (1953).....	1, 31
<u>Hafner v. Hafner</u> , 237 Minn. 424, 427, 54 N.W.2d 854, 857 (1952)	28
<u>Hecker v. Stark County Soc. Serv. Bd.</u> , 527 N.W.2d 226 (N.D. 1994).....	1, 26
<u>In Re Enger's Will</u> , 225 Minn. 229, 243, 30 N.W.2d 694, 703 (1948)	32, 35
<u>In the Matter of the Work Family Trust</u> , 260 Iowa 898, 15 N.W.2d 490 (1967)	1, 37
<u>Johnson v. Freberg</u> , 178 Minn. 594, 597, 228 N.W. 159, 159-60 (1929).....	34
<u>Johnson v. Johnson</u> , 212 N.J. Super. 368, 515 A.2d 255 (1986)	1, 34
<u>Johnson v. Johnson</u> , 272 Minn. 284, 137 N.W.2d 840 (1965)	34
<u>Knox v. Knox</u> , 222 Minn. 477, 450, 25 N.W.2d 225, 229 (1946)	28
<u>Lineback v. Stout</u> , 79 N.C. App. 292, 297, 339 S.E.2d 103, 107 (1986)	27
<u>Malcolmson v. Goodhue Cty. Nat'l Bank</u> , 198 Minn. 562, 272 N.W. 157 (1937)	2, 40
<u>Matter of Eberhart</u> , 171 Misc.2d 939, 656 N.Y.S.2d 159 (1997)	1, 33
<u>Meagher v. Hennepin Cty. Welfare Bd.</u> , 300 Minn. 446, 454, 221 N.W.2d 140, 144 (1974)	28
<u>Pine Island Farmers Coop v. Erstad & Reimer, P.A.</u> , 636 N.W.2d 604 (Minn. App. 2001), <u>aff'd</u> , 649 N.W.2d 444 (Minn. 2002)	34
<u>Plain v. Plain</u> , 307 Minn. 399, 403, 240 N.W.2d 330, 332-33 (1976).....	27
<u>Rogers v. Moore</u> , 603 N.W.2d 650, 656 (Minn. 1999).....	24

<u>Samuel v. King</u> , 64 P.3d 1206 (Or. App. 2003).....	1, 37
<u>Smith v. Tolverson</u> , 190 Minn. 410, 252 N.W. 423 (1934).....	1, 34, 39
<u>State ex. rel. Minnesota Loan & Trust Co. v. Probate Court</u> , 129 Minn. 442, 152 N.W.845 (1915).....	28
<u>Stein v. Kemp</u> , 132 Minn. 44, 155 N.W. 1052 (1916).....	36
<u>Striegel v. South Dakota Dep't of Social Servs.</u> , 515 N.W.2d 245, 247 (S.D. 1994)	27
<u>Sutliff v. Sutliff</u> , 515 Pa. 393, 528 A.2d 1318 (1987).....	1, 33
<u>Troseth v. Troseth</u> , 224 Minn. 35, 36, 28 N.W.2d 65 (1947)	38
<u>Village of Monticello v. Citizens State Bank of Monticello</u> , 180 Minn. 418, 230 N.W. 889 (1930)	36

Statutes

Minn. Stat. §501B.14	1, 25, 26, 27, 28, 29, 30, 31, 32
Minn. Stat. §501B.16	2
Minn. Stat. §519.05	1, 27
Minn. Stat. §524.6-208.....	28

Other Authorities

20 <u>Dunnell Minn. Digest</u> , Equity §102	34
Bogert, <u>Trust & Trustees</u> §923, at 451 (2d ed. 1995)	36
Bogert, <u>Trust & Trustees</u> §963 (2d ed. 1980)	34
Restatement (Second) of Trusts §187	34
Rounds <u>Loring A Trustee's Handbook</u> §6.1.3, at 236-44 (2005)	32, 36
Rounds, <u>Loring A Trustee's Handbook</u> §7.2.3.1, at 379 (2005)	39
Rounds, <u>Loring A Trustee's Handbook</u> §7.2.3.4 (2005)	40

Rules

Minn. R. Civ. Pro. 52.01 24

STATEMENT OF THE LEGAL ISSUES

1. Did the Trial Court err by approving Respondent's use of Trust assets to pay for Naomi Margolis' nursing home expenses as an appropriate expense of that Trust when (i) Respondent was disqualified from using his discretion as trustee in such a manner by Minn. Stat. §501B.14, subd.1(2); (ii) was barred from obtaining such relief by his unclean hands; (iii) acted out of an improper purpose; (iv) failed to follow the Trust Agreement and (v) violated his fiduciary duty of loyalty to the trust beneficiaries in the process?

Trial Court Ruling:

The Trial Court approved Respondent's accounting which sought to impose on the Trust the sole obligation for such expenses.

Apposite Cases and Statutory Provisions:

Matter of Eberhart, 171 Misc.2d 939, 656 N.Y.S.2d 159 (1997)
Hecker v. Stark County Soc. Serv. Bd., 527 N.W.2d 226 (N.D. 1994)
Sutliff v. Sutliff, 515 Pa. 393, 528 A.2d 1318 (1987)
Johnson v. Johnson, 212 N.J. Super. 368, 515 A.2d 255 (1986)
Conway v. Emeny, 139 Conn. 612, 96 A.2d 221 (1953)
Smith v. Tolverson, 190 Minn. 410, 252 N.W. 423 (1934)
Minn. Stat. §501B.14
Minn. Stat. §519.05

2. Did the Trial Court err when it found that Appellant failed to make a sufficient showing to require the Trustee to Explain or Account for Trust Assets?

Trial Court Ruling:

The Trial Court found that Appellant failed to meet his burden of proof to show that the Grantor intended that a Norwest Bank CD was to become part of her Trust, and that Respondent was not required to account for this asset.

Apposite Cases and Statutory Provisions:

Burgeois v. Hurley, 392 N.E.2d 1061 (1979)
Samuel v. King, 64 P.3d 1206 (Or. App. 2003)
In the Matter of the Work Family Trust, 260 Iowa 898, 15 N.W.2d 490 (1967)

3. Did the Trial Court err in approving the accounting filed by Respondent and discharging him as trustee upon the payment of \$1,518.48?

Trial Court Ruling

The Trial Court allowed the Trustee's accounting.

Apposite Cases and Statutory Provisions:

Malcolmson v. Goodhue Cty. Nat'l Bank, 198 Minn. 562, 272 N.W. 157 (1937)

STATEMENT OF THE CASE

This is an action arising under Minn. Stat. §501B.16, for an accounting by Respondent Jack Margolis as trustee of the Naomi Margolis Revocable Trust (the "Trust"), to confirm the appointment of Appellant as trustee, remove Respondent Jack Margolis as trustee, and for redress for Respondent's breaches of fiduciary duty. AA 1-9. By Order dated September 13, 2005, the Trial Court confirmed Barry Lorberbaum as trustee, noted Respondent Jack Margolis' resignation as trustee and ordered an accounting by Respondent, over Respondent's objection. AA 16-17. On October 28, 2005, Respondent filed an accounting with the Trial Court, to which Appellant objected. AA 18-26.

This is an appeal from a judgment entered May 2, 2006, based on Findings of Fact and Conclusions of Law and Order for Judgment ("Findings") of the Ramsey County District Court, the Honorable Margaret M. Marrinan. The Trial Court's Findings granted limited relief to Appellant, and allowed the accounting filed by Respondent on the condition that Respondent pay to the Naomi Margolis Revocable Trust the sum of \$1,518.80. The Trial Court's Findings otherwise denied (or never considered) Appellant's claims that Respondent breached fiduciary duties as trustee, that Respondent's accounting failed to account for certain assets that were assets of the Trust, or otherwise improperly characterized entries in the accounting as expenses of the Trust,

or allowed Respondent to be reimbursed by the Trust. Appellant requested restitution in an amount in excess of \$300,000.

This case involves the actions of Respondent Jack Margolis, who functioned as a trustee of a trust formed by his wife (Naomi Margolis), in a setting involving a second marriage, where two of the beneficiaries of the Trust were his wife's children. In reaching its decisions to deny Appellant relief for almost all of what was sought, the Trial Court all but ignored a course of conduct on the part of Respondent which violated his duties as trustee and overwhelming evidence of an improper motive on the part of Jack Margolis to deny Appellant and another beneficiary economic benefits under their mother's trust.

On March 17, 2006, before the Trial Court issued its Findings and before this appeal was taken, Jack Margolis died. Sherry Huff has been appointed Special Administrator of the Estate of Jack Margolis and the parties have filed a stipulation regarding her substitution as a respondent.

STATEMENT OF FACTS

Jack Margolis married Naomi Margolis in 1979, a marriage that lasted over 24 years. AA 28, Margolis Dep., pp. 7-10. This was the second marriage for both of them, and both Jack and Naomi had children by a prior marriage. AA 28. Naomi Margolis died in February of 2004. AA 28.

In 1994, both Jack and Naomi Margolis set up separate trusts as a part of their joint estate planning. Both of their wills poured all their assets, except for tangible personal property, into their respective trusts. AA 29, Exh. 50. Under the Naomi

Margolis Revocable Trust (hereinafter the "Trust"), Naomi Margolis was the Grantor, and Naomi and Jack Margolis were named as Trustees of the Trust. AA 29. Naomi Margolis' Will named Jack Margolis as personal representative. Exh. 50. Naomi Margolis' tangible personal property, including jewelry, clothes and other belongings, were devised to her children, Barry Lorberbaum and Marlee Burns, under the Will. Id. The Naomi Margolis Trust Agreement (hereinafter "Trust Agreement") provided that the assets of the Trust remaining after any lifetime distributions made under the Trust Agreement would pass upon Naomi's death to her children, Barry Lorberbaum and Marlee Jo Ortego, now Marlee Jo Burns. AA 30, 58.

The Jack Margolis Revocable Trust was also established on June 28, 1994, and later modified. AA 30, Exs. 51, 10 and 11. Both versions provided that upon his death, if Naomi Margolis survived him, a significant portion would pass to Naomi Margolis. Exh. 51; Exs. 10 and 11. The other beneficiaries of the Jack Margolis Revocable Trust were the children from his first marriage - Sherry Huff, Randy Margolis, Barry Margolis, and Jeffrey Margolis. AA 30. Naomi Margolis was a co-trustee under the Jack Margolis Revocable Trust until 2002, along with Jack Margolis. Exs. 51, 10, 11.

The Margolis' estate planning in 1994 and their course of conduct thereafter in placing assets into joint accounts operated to abandon the provisions of an Antenuptial Agreement entered into at the time of their marriage. AA 28-29, Exh. 1. The 1994 joint estate planning departed from the plan set forth in the Antenuptial Agreement fifteen years before. Section Five (f) of the Antenuptial Agreement provides that its provisions do not apply to joint property of the parties acquired after solemnization of the marriage.

Id. During the course of their marriage, Naomi and Jack Margolis held significant assets in joint accounts, assets which according to the Antenuptial Agreement, were not covered by its provisions.

The Naomi Margolis Revocable Trust Agreement provided that the trustees had the power to distribute income and principal to the Grantor. Section 8.3 of the Trust Agreement provided that no trustee, except for the Grantor, could exercise any discretion to distribute income or principal to himself. AA 77.

Assets Held by the Naomi Margolis Revocable Trust

Jack Margolis was a partner in the Margolis Brothers Nursery, and had been an investor for many years. AA 30. Jack and Naomi accumulated significant wealth in the course of their marriage. AA 30. During their marriage, Respondent transferred certain assets to Naomi Margolis, which were then transferred to her Trust. AA 30, Exh. 2-8. These included minority interests in three partnerships that owned shopping or retail centers, Knollwood, Ridgehill, and Rosewood. AA 30. From 1994 through October 2003, these partnerships periodically made cash distributions to the Trust. AA 31. Assets were also transferred into an account in the name of the Trust at Piper Jaffray. AA 31, Exh. 13 and 14. Certificates of Deposit at North Star Bank were also held in the name of the Trust. AA 31, Exh. 12.

There is now no dispute that these assets (the Knollwood, Ridgehill and Rosewood partnership interests, the Piper account and the NorthStar certificates of deposit) were all titled in and held in the name of the Trust prior to Naomi's death. However, after Naomi Margolis' death, Jack Margolis, in his capacity as Trustee of the Trust, represented (either

directly or indirectly) to the trust beneficiaries that none of these assets were ever held in the name of the Trust. Exh. 15, 18. This conduct on the part of a trustee, who has duties of full disclosure, went unmentioned by the Trial Court in its Findings.

Respondent Failed to Account for the Proceeds of a \$100,000 CD Which was Part of the Trust.

In 1996 or 1997, Naomi Margolis gave two pages of notes to her son, Barry Lorberbaum. T. 52. The notes were in Naomi's handwriting. Id. These notes, Exhibit 16, list under the term "Trust forwarded" and under "Naomi" the following assets:

North Star Bank	X	
Ridgehill	X	
Rosewood (Marco Mgmt)		
Knollwood (Galles)	X	
Norwest CD	X	100,000 only
Piper Jaffray	X	

There are several investments listed under "Jack" in these same notes. Jack Margolis testified that these notes accurately reflected assets held in his name. Margolis Dep., p. 78.

Prior to the mid-1990's, Naomi Margolis had worked as a bookkeeper in a variety of jobs, including employment as a bookkeeper at Margolis Brothers Nursery. T. 43. Barry Lorberbaum testified that Jack had told him that Naomi did a good job keeping track of their investments, interest payments on investments, and that they had purchased a computer so she could do so. T. 43. Miles Locketz, a certified public accountant who prepared income tax returns for Jack and Naomi Margolis handled the parties' taxes, testified that until a couple years before her admission to the nursing home, Naomi Margolis would attend a meeting each year with Jack in connection with the preparation

of their income tax return, and that at such meetings, she was "very knowledgeable" about the couple's assets. Locketz Dep., p. 27.

The second page of Naomi Margolis' notes reflect a Norwest CD number 1191946, and a reference to \$100,000. AA 85. Exhibit 17 reflects that a CD in the amount of \$100,000 was held jointly in the name of Jack or Naomi R. Margolis issued February 22, 1990, which matured on February 22, 1994, and which was identified as Certificate No. 4101191946. Certificate No. 40101191946 has the same last ten digits as the CD number listed in Exhibit 16. AA 84-85.

Another document, also part of Exhibit 17, indicates that CD No. 4101191946 was placed in the name of Jack Margolis on February 22, 1994, and this CD was scheduled to mature on July 22, 1995, about a year after the creation of the Trust in June 1994. Margolis Dep., p. 78. Respondent, however, testified in reference to Exhibit 17 that with the exception of the Knollwood, Rosewood and Ridgehill properties, "[e]verything was joint with the exception of those three pieces." Margolis Dep., p. 81-82. Wells Fargo, formerly Norwest Bank, pursuant to a document retention policy, destroyed any records pertaining to the CD or its proceeds. Exh. 58.

At the time Naomi Margolis gave Exhibit 16 to Barry Lorberbaum, she told him "These are a list of things that will go to you and your sister". T. 52. The only documentation that exists as to whether this asset was held in the name of the Trust are Naomi Margolis' own notes, which are accurate in every other respect. AA 84-85. Naomi Margolis' notes reflect the existence of a \$100,000 CD which was a part of her Trust. AA 84-85. The only way assets could pass from Naomi to her children was

through her Trust. Exh. 9 and 50. Both Jack and Naomi had been advised by their lawyer in 1994 that their assets should be held in their respective trusts. Exh. 53. By her notes, actions, and words, and other circumstantial evidence, Naomi Margolis, who was in charge of keeping track of the family assets, intended that this \$100,000 Norwest CD or its proceeds be an asset of her Trust, and represented to her son that it was a Trust asset.

Jack Margolis refused to explain or provide documentation on what happened to the proceeds of the CD Naomi Margolis listed as an asset of her Trust:

- “Q. What I’m asking you is, do you recall what happened to that hundred-thousand-dollar CD that expired in 1995?
- A. I don’t know.
- Q. All right. At that point in time, did it --
- A. I might have invested it. I don’t know. I really don’t know.
- Q. At that point in time --
- A. It was my money, you know what I mean? So I don’t know.
- Q. At that point in time did you put that hundred thousand dollars in the name of the Naomi Margolis Revocable Trust?
- A. No, I did not.
- Q. So are you testifying that the reference to this Norwest hundred-thousand dollar CD on Exh. 16 is --
- A. Shit.
- Q. -- is wrong?
- A. I don’t know whether it’s right or wrong or anything else, but she never had a dime in it.”

Margolis Dep., pp. 80-81.

Naomi Margolis’ notes, words and actions infer that she and Jack Margolis had agreed that the \$100,000 CD in Norwest was a part of the Naomi Margolis Revocable Trust. Jack Margolis never addressed the issue of his and Naomi’s specific communications on this subject, never provided any explanation as to why her notes were

accurate in every respect but wrong on the issue of the Norwest CD, never explained or produced records as to what happened to the proceeds of the CD that existed and how or whether the proceeds benefited Naomi Margolis, and misrepresented at some point that every other asset listed in her notes as part of her trust had never been so held.

Naomi Margolis' Admission to the Sholom Home.

Jack Margolis was in charge of financial and investment decisions after his wife's admission to a nursing home in 2001. Margolis Dep., pp. 51, 42. As he put it, "[i]t was my money". Id., pp. 51, 81. On May 18, 2001, Naomi Margolis was admitted to the Sholom Home, a nursing home facility. AA 32. In connection with that admission, Jack Margolis signed an Admission Agreement with the Sholom Home for the care of Naomi Margolis, which stated, on the last page:

• **RESIDENT'S SPOUSE:** _____
("Spouse")

The spouse by signing above, acknowledges joint and several responsibility for payment of all charges."

AA 33, Exh. 27. Jack Margolis' signature appears on the line for Resident's spouse. AA 33, Exh. 22. Naomi Margolis did not sign the Admission Agreement. AA 33, Exh. 27. No one signed under the "Financial Obligation of Guarantor" section of the Agreement. AA 33, Exh. 27. When Jack Margolis entered into the Admission Agreement with the Sholom Home, he assumed a personal contractual obligation to pay the nursing home expenses of Naomi Margolis to the Sholom Home. Exh. 27. The Sholom Home has confirmed that \$194,089.85 in charges not covered by insurance were paid on behalf of Naomi Margolis from 2001 through her death. AA 34, Exh. 60.

While payment for the nursing home and medical expenses was made from the joint marital checking account, in his accounting, Jack Margolis claimed that Trust income and distributions which were commingled into this account should be utilized as the sole source for payment on these expenses (and, in addition, that he should be reimbursed for amounts paid out of this joint account). In essence, while the parties' jointly held funds were improperly commingled with Trust income and distributions, Jack Margolis claimed and the Trial Court erroneously agreed that the Trust should bear the sole burden of paying these expenses.

Jack Margolis Consistently Failed to Follow the Trust Agreement -- in Obtaining an Opinion of a Competent Medical Advisor Which was a Condition for the Application of Section 2.2 of the Trust Agreement, in Involving the Other Beneficiaries in that Process, and in Failing to Have a Successor Trustee Appointed for Naomi Margolis.

Section 2.2 of the Trust Agreement provides:

“2.2 Payments in the event the Grantor becomes incapacitated. At any time while the Grantor, in the opinion of the Trustees and a competent medical advisor, is incapacitated through illness or any other cause, the Trustees shall pay to or expend for the benefit of the Grantor, and the Grantor’s issue such sum or sums from either the net income from or the principal of the Trust Estate as the Trustees, in the Trustees’ discretion, may deem necessary or advisable to provide for the proper support, maintenance, and health of the Grantor, and the Grantor’s issue.”

Exh. 9 (emphasis added). Jack Margolis admitted that he never followed the Trust Agreement direction to obtain an opinion of a competent medical advisor regarding Naomi Margolis' condition. Margolis Dep., p. 47-48. The term “incapacitated” is not defined in the Trust Agreement.

Section 8.7 of the Trust Agreement provides in part as follows:

“8.7 Disability of Trustee. At any time while any Trustee acting hereunder, in the opinion of the other Trustee or Trustees then acting hereunder and a competent medical advisor nominated by a majority of the group consisting of the Grantor’s living adult issue, is incapacitated through illness, age or other cause, such other Trustee or Trustees shall have full power and authority”

Exh. 9, p. 21 (emphasis added). The Trust Agreement’s reference to the competent medical advisor in Section 8.7, as in Section 2.2, contemplates a process whereby Naomi Margolis’ children, who were also beneficiaries, would participate in selecting a competent medical advisor and obtaining an informed medical opinion regarding Naomi’s condition, which was a prerequisite for the operation of Section 2.2 of the Trust Agreement.

Jack Margolis never contacted the beneficiaries of the Trust to inform them of this process, or to obtain an informed medical opinion on whether Naomi Margolis was incapacitated. T. 49. Jack Margolis failed to follow the terms of the Trust Agreement in obtaining the opinion of a competent medical advisor and in obtaining the input and consent of Barry Lorberbaum and Marlee Burns in that process.

Naomi Margolis remained a trustee of her Trust until her death. AA 33. No action was taken in 2002 or thereafter to remove Naomi as trustee of her own Trust, or to have a successor trustee appointed, even though it was clear to Jack Margolis that she was not capable of exercising trustee functions, and even though he took action to have her removed as trustee of the Jack Margolis Revocable Trust in 2002. Margolis Dep., pp. 42-44.

The Trust Agreement, in Section 8.1 (Ex. 9, p. 18), specifically includes a provision for the appointment of a successor trustee if Naomi Margolis was unable to serve:

“If for any reason NAOMI MARGOLIS is unable or unwilling to continue to serve as a Trustee hereunder, then NAOMI MARGOLIS may designate an alternate or successor Trustee. Such designation shall be in writing signed by NAOMI MARGOLIS, and said designated individual shall become a Trustee hereunder at such time as provided in said writing and upon filing a written acceptance of such office with the trust records. If NAOMI MARGOLIS fails to designate an alternate or successor Trustee as provided above, then the Grantor’s son, BARRY LORBERBAUM, shall become a Trustee hereunder by filing a written acceptance of such office with the trust records.”

AA 33, 75. There is no evidence that Naomi Margolis designated a successor trustee other than Barry Lorberbaum. AA 33, 75. Despite having numerous opportunities to do so on Appellant’s visits to Minnesota, Jack Margolis never contacted Barry Lorberbaum and asked him to act as successor trustee pursuant to the Trust Agreement. AA 33, Margolis Dep., p. 47; T. 47. Jack Margolis testified he did not see any need in replacing Naomi as a trustee if he was handling the trust. Margolis Dep., p. 47. Had Barry Lorberbaum been advised of the opportunity during Naomi’s lifetime to become a successor trustee of the Trust, he would have accepted the position. T. 47.

Respondent’s failure to involve the beneficiaries in the process contemplated by the Trust was a significant breach. It deprived the beneficiaries of the structural protections of the Trust Agreement, and it left Jack Margolis, burdened with conflicts of interest, free to make all decisions involving the Trust.

When Jack Margolis Used Trust Income and Assets to Pay Naomi Margolis’ Nursing Home Expenses, He Used His Discretion under the Trust Agreement to

Indirectly Benefit Himself, And Discharge His Duty of Support and Relieve His Personal Obligations.

Throughout the time Jack Margolis acted as Trustee of the Trust, at least until the end of 2003, the real estate partnerships in which the Trust was a partner, made cash distributions to the partners. AA 33-34. Distributions and other income generated by the Trust assets were never deposited in separate accounts by Jack Margolis. AA 34. Rather, cash distributions from the partnerships to the Trust were generally deposited into a Wells Fargo savings/checking account held in the names of Jack or Naomi Margolis. AA 34. This was a joint account. AA 34. Margolis Dep. pp. 52-54; see, Exh. 28.

When Jack Margolis made the decision to pay the Sholom Home, he had four basic options: he could use his own personal funds, he could use Trust funds, or he could use his and Naomi's jointly-owned marital assets, or some portion of any of these. When he made the decision to use Trust assets, either at the time he wrote the checks or years later when he filed his Accounting with the court in 2005, he used his discretion as Trustee of the Naomi Margolis Revocable Trust under Section 2.2. If that section was operative for such a purpose, as Trustee, he could have used his discretion to determine how much, if any, of the Trust funds should be devoted to pay the Sholom Home, and for whose benefit (Naomi, Marlee, or Barry) the principal and income of the Trust should be used. Section 2.2 undeniably empowers the Trustees with discretion to make these judgments.

Jack Margolis had a conflict of interest in connection with his decision making with respect to what funds or assets to use to pay the bills of the Sholom Home from

2001 to Naomi Margolis' death. At the time, he owed a duty of undivided loyalty to Barry Lorberbaum and Marlee Burns under the Trust. If he used Trust funds to pay the nursing home and medical expenses, he depleted Trust assets but avoided using his personal funds, or other jointly-held assets or funds (in which he also had an interest) which Naomi had the power and right to use. When he made these decisions, he was contractually obligated to the Sholom Home to make the payments, and was under a legal duty of support as a husband to pay for his spouse's medical care.

Jack and Naomi Margolis had ample assets other than Trust assets to cover the nursing home and medical expenses paid to the Sholom Home. At the end of 2000, the Jack Margolis Revocable Trust held assets in excess of \$2 million. See, Exh. 35-37. At the end of 2000, just prior to Naomi Margolis' admission to the nursing home, the joint checking and savings accounts held in the names of Jack and Naomi Margolis at Norwest, now Wells Fargo, had a balance of \$863,121.44. Margolis Dep., Exh. 28. In addition, there were other joint accounts held in Jack and Naomi's names which held assets as of the year-end 2000 of approximately \$50,000. Margolis Dep., Exs. 29, 30, 31, 32, 33 and 34. Thus, Jack and Naomi Margolis had over \$900,000 in jointly-held marital assets shortly before any nursing home expenses began to be incurred.

The November 2003 Assignments of Trust Assets to the Jack Margolis' Trust

The periodic cash distributions paid to the Naomi Margolis Revocable Trust were made in the form of checks payable to the Trust. AA 33-34. These payments were received by Jack Margolis after Naomi Margolis was admitted to the Sholom Home. From the 1990s until the end of 2003, Jack and Naomi Margolis received 1099s from

Piper Jaffray and the North Star Bank, and each year received K-1s from the three partnerships, in the name of the Naomi Margolis Revocable Trust. AA 34. After Naomi Margolis resided in the Sholom Home, Jack Margolis received the 1099s on her behalf. AA 34.

In November of 2003, the Knollwood West Partnership distributed some mortgage refinancing proceeds to its partners. AA 35. The Trust received a check in the amount of Fifty Thousand Four Hundred Seventy-Four Dollars (\$50,474). Exh. 26. Jack Margolis deposited this check in the joint checking account owned by he and Naomi. AA 35.

Shortly after receiving this check, in November of 2003, Jack Margolis testified he discussed with his attorney, Kathleen Doar of the Parsinen firm (one of the attorneys at this firm had drafted the Trust in 1994), moving the real estate partnership assets in the Trust to the Jack Margolis Revocable Trust. AA 35, Margolis Dep., p. 31, 101. In this time frame, Naomi's death was regarded as imminent. AA 35, p. 138.

In November of 2003, Jack Margolis authorized his daughter, Sherry Huff, to work on his behalf with Kathleen Doar, his lawyer, on these asset transfers. T. 8-9, 14, 23. Acting on his authority, Sherry Huff corresponded with Kathleen Doar about these matters, and kept Jack Margolis informed by giving him copies of Ms. Doar's e-mails and her letters, or by reading Ms. Doar's responses to her father. T. 24.

Jack Margolis expressed his motivation in having the Trust assets transferred to him was to insure that Naomi's children got nothing from her death. Exh. 52. Among other things, this is corroborated by Sherry Huff's communication to Ms. Doar dated November 14, 2004, where she quoted Jack Margolis as stating: "I worked hard my

whole life and I have nothing for her kids”. Id. At the same time, he told Ms. Huff, who told Ms. Doar, that he wanted Naomi’s share of the Knollwood, Ridgehill and Rosewood limited partnership interests (held in the Trust) “transferred to him under the trust”. Id.

In response to Ms. Huff’s questions and Jack Margolis’ requests, Ms. Doar, sent an e-mail on November 19, 2003:

“He can use his power as Trustee of Naomi’s Revocable Trust, acting alone pursuant to the delegation, to transfer assets from her Revocable Trust to his Trust. He runs a risk moving assets from her trust to his that her children will argue that he ‘took’ her assets. Therefore, I am sending an action by Trustee with the other documents today for your father’s review and signature to support his action on those assets.”

Exh. 55 (emphasis added). The form sent by the attorney transferred the assets of the Trust to the Jack Margolis Revocable Trust. Exhibit A to the Action by Trustee form identified the Ridgehill, Knollwood, and Rosewood partnership interests owned by the Trust, as well as real estate and some Wells Fargo accounts which were not held by the Trust. AA 36, Exh. 20 and 21. Jack Margolis signed Exhibit 21, with the attached Exhibit A. AA 36.

Jack Margolis testified that he knew Barry Lorberbaum and Marlee Burns were beneficiaries of the Trust. Margolis Dep., p. 144-45. Jack Margolis agreed that the transfer of the remaining assets of the Naomi Margolis Revocable Trust to the Jack Margolis Revocable Trust did not benefit the beneficiaries of the Trust. Id., pp. 129-30. No one disclosed to the beneficiaries of the Trust that all the assets of the Trust had been removed by Respondent, its Trustee, to the Jack Margolis Revocable Trust.

Jack Margolis knew that the Ridgehill, Rosewood, and Knollwood partnership interests were held in the Trust, i.e., that they were Trust assets. Jack Margolis was involved in allocating these interests to Naomi's Trust, he regularly received distribution checks payable to the Trust, as well as 1099s and other partnership correspondence referring to the Naomi Margolis Revocable Trust. These checks were periodically received by Jack Margolis, and Naomi's name would be signed to endorse the check. See, Exh. 26. The correspondence between Ms. Doar and Sherry Huff also refers to the partnership assets as Trust assets. Jack Margolis also had to know that when all the assets were transferred out of the Trust in November of 2003, this action was not in the best interests of the beneficiaries of the Trust.

The actions of Jack Margolis in transferring assets out of the Trust to the Jack Margolis Revocable Trust, as well as the use of Trust assets as the sole source to pay nursing home expenses, were motivated by his bias against one of the beneficiaries, and his desire to benefit a favored set of beneficiaries, his own children. This conclusion is confirmed by his own statements, including statements made to Sherry Huff as reflected in Exhibits 52 and 54. In addition, Barry Lorberbaum testified that on two occasions, Jack Margolis made comments reflecting an unmistakable bias against Marlee Burns. On one occasion, apparently disappointed over Marlee not visiting her mother in the nursing home, Jack Margolis told Barry Lorberbaum that hell would freeze over before Marlee would receive anything from Naomi's estate. T. 50. On another occasion, Jack Margolis told Barry Lorberbaum that Marlee Burns would not obtain Naomi's wardrobe after her death, despite the fact her Will provided for such a bequest. T. 50; Exh. 50.

Not only were Jack Margolis' statements to others reflective of his bias towards one of the Trust beneficiaries, his own testimony reflects that the motivation for the asset transfers from the Trust to his trust was because of his bias:

- “Q. Is it fair to say over the years you really didn't talk to Barry Lorberbaum about financial aspects involving Naomi? Is that fair?
A. Not too much. No. But I used to see him. He used to come here once a month and stay with me.
Q. And he would visit his Mom?
A. Huh?
Q. He would visit his Mom when he was here?
A. Yeah, he's the only one that visited. Her daughter never did. Once in four years.
Q. You were unhappy about that?
A. Well - it's her Mom. What we didn't do for that girl. Bought her a couple of cars.
Q. And Naomi would send her some money once in a while?
A. Almost every month.
Q. And that stopped in the mid-1990's or so?
A. I suppose.
Q. You never sent her any money?
A. I sent her money too.
Q. Did you send her money after --
A. At Nome's insistence. I wouldn't give her the right time of day.
Q. So you were unhappy with her?
A. Very unhappy with her. She married three or four times.
Q. So was part of this moving assets around because you were very unhappy with Marlee?
A. Very unhappy with her.
Q. And part of why some of this went on with the assignments and so on, that that had -- at least partway -- had something to do with Marlee, and you being unhappy with her?
A. Very unhappy with her.
Q. Are you agreeing with me?
A. Yeah.”

Margolis Dep., pp. 127-29 (emphasis added). It is obvious that Jack Margolis motives to deny Naomi's children whatever he could in the event of her death motivated his conduct in 2003 and beyond, including the allocations used in his Accounting with regard to

nursing home expenses. The Trial Court, however, made no findings regarding Respondent's motivation.

In 2004, after Naomi Margolis' death and an exchange of information occurred between attorneys for the parties, Respondent's attorney wrote a letter dated October 28, 2004, where she indicated that she had "now verified" that the Trust owned a 12.619% interest in Knollwood West Partners, an 8.33% interest in Ridgehill Partners, and a 7.5% interest in Rosewood Center Partners. AA 38, Exh. 25. Ms. Doar characterized the November 2003 assignments as "legally ineffective" and indicated that the partnerships had been notified to restore the ownership of the partnership interests assigned in November 2003 back to the Trust. AA 38. Distributions received thereafter from the partnerships for the Trust have generally been sent to Appellant's attorneys. AA 38. The Ridgehill distributions were first received in December of 2004, and distributions from the other partnerships began in 2005. AA 38. The three real estate partnership interests were transferred back to the Trust in 2004 prior to the commencement of this litigation in 2005. AA 38.

Jack Margolis' Has Retained Partnership Distributions After Her Death Which Should Have been Paid to the Naomi Margolis Revocable Trust.

Ms. Doar's letter, Exhibit 25, also indicated that an accounting of the expenses after her death would be made, and that Jack would "reimburse the trust with the net balance due". This reimbursement has never occurred. AA 38, T. 64. After Naomi Margolis' death in February of 2004 until the end of 2004, the Jack Margolis Revocable Trust received the sum of \$29,263.65 in cash distributions from the Knollwood,

Rosewood and Ridgehill partnerships before Appellant began receiving partnership distributions. AA 40. Absent the November 2003 assignments which transferred the Trust's partnership assets to the Jack Margolis Revocable Trust, this sum would have been received by the Trust. AA 40.

Jack Margolis has never provided a good faith explanation to justify his retention of the \$29,263.25 received since Naomi Margolis' death. There were no nursing home expenses to offset these proceeds against, and he had an ongoing obligation to restore these funds to the Trust. These distributions were property of the Trust, there was no expense to apply these to after Naomi's death, yet the Trial Court improperly allowed Respondent a credit for these funds in his Accounting.

Jack Margolis' Misleading Representations as to Trust Matters

After Naomi Margolis' death in 2004, Barry Lorberbaum asked and wrote Jack Margolis about matters involving her estate, including the Trust Agreement that he had seen nearly a decade before. Exh. 19. Jack Margolis, although Trustee, ignored these requests. Margolis Dep., pp. 90-91; T. 62.

In September of 2004, attorneys for Mr. Lorberbaum inquired of Respondent's attorney regarding the status of Naomi Margolis' estate. In response to these inquiries, Kathleen Doar wrote a letter dated September 7, 2004, where she indicated "I do not believe that Naomi's Revocable Trust was funded" Exh. 18. Jack Margolis knew of the three partnership interests that were formerly held in the name of the Trust, as well as other accounts that had been held in the name of the Trust. He had previously been advised by his lawyer that he might be accused of taking Trust assets if he had them

transferred to him in 2003. Ex. 55. As of September of 2004, the partnership interests owned by the Trust had been transferred to Jack Margolis' trust, on forms prepared by the his lawyer's firm and signed by Jack Margolis, approximately one year earlier. See, Exh. 21. Jack Margolis received a copy of Exhibit 18, read it at the time, but took no action to correct the misstatement that the Trust had not been funded:

- “Q. And you got a copy of this letter, right? It says cc to Jack Margolis.
A. Yeah.
Q. And you would have gotten a copy of this September 2004 sometime, right?
A. I don't remember.
Q. Well, do you have any reason to believe you didn't get it?
A. I got it.
Q. And this has that statement in it in line number 3, “I do not believe Naomi's Revocable Trust was funded.” Do you see that reference there?
A. Um-hmm.
Q. And did you read the letter when you got it in September of 2004?
A. I must have, yeah.
Q. And did you tell Ms. Doar that the statement about the Naomi Margolis Revocable Trust not being funded was incorrect?
A. I don't remember.
Q. Well, you knew it wasn't correct because --
A. I don't know. I don't remember.
Q. All right. Well, you knew at the time --
A. Ah, shit.
Q. * * * You knew in September 2004 that the statement that the Naomi Margolis Revocable Trust was not funded was wrong because you knew about the partnership interests being in the name of the Naomi Margolis Revocable Trust?
A. I don't remember.
Q. You don't remember? Okay.
Did you talk to anybody in September of --
A. I never talked to anybody.”

Margolis Dep., p. 86-88.

During the course of this proceeding, in response to inquiries by the beneficiaries of the Trust and the successor trustee (Appellant) as to the other assets that were held in the name of the Trust, Jack Margolis provided an Affidavit, through attorneys at the Parsinen firm. Exh. 15. This Affidavit states:

“Aside from the partnership interests in Rosewood Center Partners, Knollwood West Partners and Ridgehill Partners, there were no other assets held in the name of the Naomi Margolis Revocable Trust, dated June 28, 1994.”

This Affidavit was made under oath. Jack Margolis was a Trustee of the Naomi Margolis Revocable Trust at the time he provided this Affidavit. The unqualified statement in the Affidavit regarding the assets of the Trust failed to mention the Norwest CD in the amount of \$100,000, the North Star Bank CDs in the name of the Trust, and the Piper Jaffray account held in the name of the Trust. Jack Margolis testified he did not look at his tax returns or other documents in providing this Affidavit, and did not remember what he did to verify the information in the Affidavit was correct. Margolis Dep., pp. 70-71.

The unqualified representation made by Jack Margolis in his Affidavit was false, misleading and incomplete, and inconsistent with his duty of full disclosure as Trustee of the Naomi Margolis Revocable Trust, but all so consistent with his pattern of conduct as Trustee -- to conceal the truth from the beneficiaries and deprive them of any economic benefit from the Trust.

Fiduciary Breaches of Trust

Jack Margolis engaged in an overall course of conduct which has breached his duties as Trustee of the Trust. In his capacity as Trustee, he has failed to follow the Trust

Agreement, used Trust funds to retire his personal obligations, improperly transferred assets of the Trust to another trust with favored beneficiaries, failed to respond to valid inquiries of the Trust beneficiaries for information concerning the Trust, improperly retained Trust assets, and misrepresented (directly or indirectly) the existence and extent of Trust assets, which was an attempt to conceal his potential liabilities as Trustee. The Trial Court ignored Respondent's misconduct as Trustee and overwhelming evidence of his motive to deny the beneficiaries any economic benefits under the Trust.

Restoration of Trust Assets to the Naomi Margolis Revocable Trust

From the beginning of 2001 until Naomi Margolis' death in February of 2004, a total of \$123,329 in the way of cash distributions were made from the Knollwood, Rosewood and Ridgehill partnerships, which were either paid to or would have been (were it not for the November 2003 assignments) paid to the Naomi Margolis Revocable Trust, and received by Jack Margolis as Trustee. AA 40. These were commingled with other funds of the parties in a joint checking account. In addition, in 2001 and 2002, Respondent received \$44,325.65 in the way of proceeds from the North Star Bank CDs owned by the Trust deposited in the parties' joint bank account. Jack Margolis never explained what happened to or accounted for the sum of \$100,000 in the way of proceeds from the Norwest CD referred to in Naomi Margolis' notes. Exh. 16.

The parties stipulated that the sum of \$10,987 from the Trust's Piper Jaffray's account was transferred into the Jack Margolis Revocable Trust in 2001. AA 31. These funds were not deposited in the joint checking account, they were transferred from Naomi's Trust to the Jack Margolis Revocable Trust and placed out of the reach of the

Trust's beneficiaries. There is no evidence that the Jack Margolis Revocable Trust ever made any payments to the Sholom Home for nursing home expenses. Inexplicably, the Trial Court failed to require Jack Margolis to make restitution of this amount to the Trust.

Appellant argued to the Trial Court that Respondent owed the Trust the sum of \$307,902.80, without interest, which represents the amount received by Jack Margolis as Trustee from the various partnerships, the transfer of the Piper funds, the funds received by the Jack Margolis Revocable Trust since Naomi Margolis' death, and the \$100,000 as proceeds of the Norwest CD which Jack Margolis failed to account for. Exh. 56. Despite the fact that Jack Margolis was disqualified from using his discretion as Trustee to make the particular payments under Minnesota law, his consistent failure to follow the Trust Agreement, overwhelming evidence of a motive to deny the beneficiaries any recovery under the Trust, and a course of conduct which consistently breached fiduciary duties and amounts to unclean hands, the Trial Court erroneously approved his accounting on the basis that he restore the sum of \$1,518.80 to the Trust.

STANDARD OF REVIEW

Minn. R. Civ. Pro. 52.01 states that, "Findings of Fact, whether based on oral or documentary evidence, shall not be set aside unless clearly erroneous." The standard of review dictates reversal of a trial court findings when, on a review of the entire record, the Court is left with the "firm and definite conviction" that a mistake was made. Rogers v. Moore, 603 N.W.2d 650, 656 (Minn. 1999); City of Minnetonka v. Carlson, 298 N.W.2d 763, 766 (Minn. 1980).

ARGUMENT

The record is filled with evidence establishing that once Naomi Margolis entered the nursing home, Trustee Margolis acted with the inappropriate purpose of depleting assets available to the beneficiaries of the Trust in an effort to unjustly enrich himself and those that stood to inherit from him upon his death. The Trial Court seemingly resolved all doubts at every turn in favor of a trustee whose conduct breached almost every fiduciary obligation a trustee owes to a trust beneficiary. Upon a review of the entire record this Court will be left with the "firm and definite conviction" that a mistake was made.

- I. **The Trial Court Erred in Allowing Trustee Margolis' Accounting, and In Approving His Request that the Trust Bear the Sole Burden to Pay the Nursing Home and Medical Expenses for Naomi Margolis.**
 - A. **The Trial Court Erred in Failing to Consider the Impact of Minn. Stat. §501B.14, Subd. 1(2) Which Disqualified Trustee Margolis from Making Distributions of Trust Assets for Nursing Home Expenses When Doing So Discharged His Legal Duty to Support His Spouse and Relieved His Personal Contractual Obligation To Pay Such Expenses.**

The Minnesota Legislature has enacted limits on discretionary powers provided to trustees under trust agreements. Specifically, Minn. Stat. §501B.14, subd. 1(2) provides:

“Subdivision 1. Prohibition. No trustee may exercise or participate in the exercise of any of the following powers:

(2) any power to make discretionary distributions of either principal or income to discharge any legal support or other obligations of the trustee to any person.”

1. **The Language Of Section 2.2 Of The Trust Agreement Clearly Reflects The Intent Of The Grantor To Establish A Discretionary Power, Therefore, Section 2.2 Is Squarely Within The Domain Of Minn. Stat. §501B.14, Subd 1(2).**

Under the terms of Minn. Stat. §501B.14 subd.1(2), Jack Margolis could not make discretionary distributions to discharge his legal support or other obligations. Section 2.2 of the Trust Agreement provides:

“At any time while the Grantor * * * is incapacitated through illness or any other cause, the Trustees shall pay to or expend for the benefit of the Grantor, such sum or sums from * * * the Trust Estate as the Trustees, in the Trustees’ discretion, may deem necessary or advisable to provide for the proper support, maintenance, and health of the Grantor, and the Grantor’s issue.”

Exh. 9 (emphasis added). Section 2.2 empowers the trustees to expend those Trust assets that the trustees, in their discretion, deem necessary or advisable. The Trustees must use their discretion to determine when and to what extent the Trust assets should be distributed. This judgment could involve a minimal amount, a more substantial amount, or even nothing. See, e.g., Hecker v. Stark County Soc. Serv. Bd., 527 N.W.2d 226, 230 (N.D. 1994) (trust agreement which provided that the trustee “shall pay” or apply for the benefit [of the beneficiary] “such amounts . . . as the Trustee in the Trustee’s sole discretion may . . . be necessary”, empowered the trustee with discretion “to determine when and to what extent that power will be exercised”, which included the power “to make no distribution at all”). Under Section 2.2, the Trustees must also exercise their discretion to allocate how much, if any, of the Trust assets are expended directly for the benefit of the Grantor, and how much for the benefit of the Grantor’s issue.

In Hecker, the trust agreement read essentially the same as Section 2.2: “The Trustee shall pay . . . to the benefit of the beneficiary . . . such amounts . . . as the Trustee in the Trustee’s sole discretion may from time to time deem necessary or advisable for

the satisfaction of the beneficiary's special needs." Id. at 228. The court held such language, even though it included the word "shall", gave the Trustee absolute discretionary power because "the trustee retains the discretionary power to determine when and to what extent [the power to distribute] will be exercised." Id. at 230; see also, Striegel v. South Dakota Dep't of Social Servs., 515 N.W.2d 245, 247 (S.D. 1994) (finding discretionary the language, "the trustee shall expend such sums . . . of the trust as he in his sole discretion deems advisable . . ."); Lineback v. Stout, 79 N.C. App. 292, 297, 339 S.E.2d 103, 107 (1986) (reference to the trustee's discretion is evidence of intent that the trustee's power is discretionary). These decisions hold, even though the agreement uses the word "shall", that the use of the word "discretion" with a power to determine to what extent trust assets are used, necessarily leads to the conclusion that the power is discretionary. The language of Section 2.2 clearly reflects the intent of the Grantor to establish a discretionary power, not a mandatory one. Thus, Section 2.2 is squarely within the ambit of Minn. Stat. §501B.14, subd. 1(2).

2. Trustee Jack Margolis Clearly Owed A Duty Of Legal Support And Was Personally Liable For His Wife's Medical Expenses.

Minn. Stat. §519.05(a) provides as follows:

"(a) A spouse is not liable to a creditor for any debts of the other spouse. Where husband and wife are living together, they shall be jointly and severally liable for necessary medical services that have been furnished to either spouse"

Under Minnesota law, it is well settled that a spouse is liable for medical expenses incurred by the other spouse. Plain v. Plain, 307 Minn. 399, 403, 240 N.W.2d 330, 332-33 (1976). Under Minn. Stat. §519.05, there is no question Jack Margolis owed a duty of

legal support and was personally liable for his wife's medical care expenses. Meagher v. Hennepin Cty. Welfare Bd., 300 Minn. 446, 454, 221 N.W.2d 140, 144 (1974) (a husband is legally responsible for the support of his wife while they are married).

The relationship between a husband and wife is "confidential in nature and fiduciary in its character." Knox v. Knox, 222 Minn. 477, 450, 25 N.W.2d 225, 229 (1946). See also, Hafner v. Hafner, 237 Minn. 424, 427, 54 N.W.2d 854, 857 (1952); State ex. rel. Minnesota Loan & Trust Co. v. Probate Court, 129 Minn. 442, 152 N.W.845 (1915). Here, the confidential nature of the relationship and his fiduciary obligations required that Jack Margolis act in good faith in discharging his duty of support to his spouse.

The evidence was clear that there were ample jointly-held marital assets, other than Trust assets, available to pay the nursing home expenses. These jointly held checking and savings accounts could have been paid, on request, to any one or more of the owners of the account, including Naomi Margolis, at any time. Minn. Stat. §524.6-208. Rather than choosing to apply jointly held marital funds to pay such expenses, Jack Margolis, in his accounting, requested that Trust assets be utilized to make such payments, and in effect imposed on the Trust the sole liability for such payments. Respondent's choice was obviously self-serving and clearly contrary to Naomi's desire to have her Trust assets pass to her designated beneficiaries. T., pp. 46, 55.

3. The Trial Court Erred In Failing To Directly Consider The Impact Of Minn. Stat. §501B.14, Subd. 1(2).

For purposes of Minn. Stat. §501B.14, subd. 1(2), Jack Margolis not only had a duty of legal support with respect to medical and nursing home expenses paid on behalf of his wife, but his contractual undertaking to the Sholom Home to pay Naomi Margolis' nursing home expenses created a type of "other obligation" envisioned by the statute as well.

Jack Margolis had significant conflicts of interest as trustee in the decision as to what source of funds to use to pay Naomi Margolis' nursing home expenses. He had of course several options - Trust assets, his own assets, or assets held jointly with Naomi of nearly \$1 million. He chose to burden the Trust with this expense, to the exclusion of any other sources of funds. The use of Trust income or assets to pay Naomi Margolis' nursing home and medical expenses relieved or reduced the extent to which Jack Margolis' assets (or joint assets which became his upon her death) were utilized to fulfill his legal support obligations or to make good on his contractual obligation to the Sholom Home. The use of discretion in this type of setting, where a trustee has discretion to indirectly benefit himself, is exactly what Minn. Stat. §501B.14 subd. 1(2) condemns as an impermissible use of a trustee's power.

Jack Margolis' request to allocate the Trust income or other assets to pay Naomi Margolis' nursing home and medical expenses before any other assets in which she had an ownership interest were used cannot be reconciled with the provisions of Minn. Stat. §501B.14, subd. 1(2). Under that provision, Jack Margolis was disqualified as trustee from exercising his discretion under Section 2.2 of the Trust Agreement in using Trust

funds which had the effect of retiring or minimizing his own contractual obligations or duty of support.

The Trial Court failed to directly consider the impact of Minn. Stat. §501B.14, subd. 1(2). In fact, the Trial Court's Findings or Memorandum do not even mention the statute. The Trial Court apparently confused Appellant's argument that Jack Margolis was disqualified under Minn. Stat. §501B.14, subd. 1(2) from acting under Section 2.2 with the notion that he failed in his duty to support his spouse. AA 51 (by funding the Trust, he satisfied his duty of support.) This is just not the point. The point is, however, that Jack Margolis could not act as a decision-maker under Minn. Stat. §501B.14, subd. 1(2) when he indirectly benefitted from how the Trust assets were, or were not allocated, with regard to the payment of nursing home expenses.

B. The Trial Court Erred When it Honored Jack Margolis' Request to Allocate the Trust Income to Pay Naomi Margolis' Nursing Home and Medical Expenses Before Any Other Assets in Which She had an Interest were Used, Because Jack Margolis is Not Entitled to Rely on Section 2.2 of the Trust Agreement Due to his Failure to Follow the Provisions of the Trust Agreement.

Respondent failed to follow the process required under the Trust Agreement to select an independent medical advisor, failed to obtain the opinion of a competent medical advisor on whether Naomi Margolis was incapacitated within the meaning of the Trust Agreement, and failed to implement the process in obtaining a successor trustee for Naomi Margolis under the Trust. All of these matters had a direct impact on how the Trust assets were to be used in the event Naomi Margolis was unable to serve as trustee because of health reasons.

A trustee who breaches his duty by not following the conditions of a trust instrument is breaching his or her duty, and any decision which flows from that breach cannot be upheld. See, Conway v. Emeny, 139 Conn. 612, 620, 96 A.2d 221, 225 (1953) (failure of trustees to comply with the standard governing their discretion of considering the public interest in closing a museum was a breach of duty, and their decision was reversed, as a “trustee’s obligation to obey the instructions of the donor of the trust is the cornerstone upon which all other duties rest”).

The Trial Court engaged in complete speculation when it concluded that had Barry Lorberbaum been appointed successor trustee years before, and he objected, a court would have approved Jack Margolis’ request to burden the Trust before any other marital joint assets were used to pay these expenses. The appointment of a successor trustee for Naomi (as required by the Trust Agreement) never happened, of course, nor was any request to the Court ever made by Appellant or Respondent. If Appellant had become successor trustee, he might just as easily have struck an arrangement with Jack Margolis where some part of the Margolis’ joint assets were used (as opposed to solely Trust assets) to pay nursing home expenses. The fact is Trustee Margolis never made such a request, never followed the Trust Agreement which contemplated the involvement of the beneficiaries, acted out of improper motives and consistently breached his duties as Trustee. The Trial Court’s indulgence in speculation to excuse in hindsight an undeserving disqualified trustee is very hard to understand. Nor is the Trial Court’s speculation consistent with the policy underlying Minn. Stat. §501B.14 subd. 1(2), which requires a fiduciary to apply to the court if he is disqualified under the statute; speculation

years after court approval should have been sought does not further the purposes of Minn. Stat. §501B.14 subd. 1(2).

Trustees are required to follow trust agreements; such an obligation is a fundamental part of being a trustee. When trustees fail to follow the trust, it is plainly wrong to give the trustee the benefit of any doubt and simply conclude, by speculating on what outcome may have resulted, that it just does not matter that the trustee breached the Trust.

C. The Trial Court Erred When It Approved Jack Margolis' Request to Allocate to the Trust the Entire Burden of Naomi Margolis' Nursing Home and Medical Expenses Because his Request Was an Integral Part of a Course of Conduct which Breached his Fiduciary Duty of Loyalty to the Trust Beneficiaries and was Motivated by an Improper Purpose.

Trustees have a duty of undivided loyalty to the beneficiaries. See, Rounds Loring A Trustee's Handbook §6.1.3, at 236-44 (2005). This duty is premised on a recognition that it is "generally, if not always, humanly impossible for the same person to act fairly in two capacities and on behalf of two interests in the same transaction." Id., at 237 (citations omitted). A trustee may not receive direct or indirect benefit from the trust unless authorized by the trust agreement, a court, or by statute. Id., p. 242. Self-dealing by a trustee involves a breach of that duty which gives rise to an equitable cause of action. In Re Enger's Will, 225 Minn. 229, 243, 30 N.W.2d 694, 703 (1948). The notion that a trustee cannot exercise his or her discretion to use income or principal of the trust in a manner which benefits himself is simply an aspect of the overall duty of loyalty, which provides that a trustee cannot directly profit or gain from his own administration of a trust.

For example, in Matter of Eberhart, 171 Misc.2d 939, 656 N.Y.S.2d 159 (1997), a court was asked to reform two revocable trusts and consider the issue whether a trustee could exercise his discretionary power of invasion to satisfy his obligation to support his children, the beneficiaries of the trust. The court stated that a trustee under New York law may not exercise a discretionary power in his own favor, and concluded that a distribution of trust assets in a manner which reduced the trustee's own financial obligations were tantamount to a direct distribution to himself. Id. In holding that such a power could not be used, the court concluded that to hold otherwise would allow for a breach of fiduciary duty, and would allow the trust to recover from the trustee individually. Id.

Similarly, in Sutliff v. Sutliff, 515 Pa. 393, 528 A.2d 1318 (1987), the Pennsylvania Supreme Court held that the father and business associate who acted as custodians under a Uniform Gift to Minors Act ("UGMA") set of accounts, who used the children's UGMA property to fulfill some part of the father's support obligation, breached their fiduciary duties and violated their duty of loyalty. Id. at 408.

Eberhart and Sutliff are just like the present situation, where the trust agreement empowers the trustee in a family setting to act in a certain way, but when he acts indirectly to benefit himself, it is an impermissible act. When Jack Margolis made the decision on what funds to use to pay the Sholom Home, he was under a significant conflict of interest, and he chose to benefit himself and burden the Trust with these expenses. Consistent with other actions he undertook as Trustee, Respondent made this decision with an improper motive, i.e., to benefit himself and disadvantage beneficiaries to whom he owed an undivided duty of loyalty. When he did so, he violated his duty of undivided loyalty to the

beneficiaries of the Trust. See, Smith v. Tolverson, 190 Minn. 410, 415, 252 N.W. 423, 425 (1934) (holding a trustee in breach of his duty of loyalty). See, Restatement (Second) of Trusts §187 cmt. f. & g. (court will intervene when trustee acts from a dishonest or improper motive).

The Trial Court made no findings regarding Respondent's motive or regarding his course of conduct, but the evidence is overwhelmingly clear that his actions were infected with a bias against the very beneficiaries to whom he owed fiduciary duties and an overriding purpose to deprive them of the economic benefits of their mother's Trust.

D. The Trial Court Erred When It Allowed Jack Margolis' Request to Allocate the Use of Trust Income or Assets to the Nursing Home and Medical Expenses, Because Jack Margolis had Unclean Hands.

One who comes into equity must come with clean hands. 20 Dunnell Minn. Digest, Equity §102 (4th ed. 1993). An accounting is an equitable proceeding. Johnson v. Johnson, 272 Minn. 284, 137 N.W.2d 840 (1965). Bogert, Trust & Trustees §963 (2d ed. 1980). A court of equity should refuse relief to a party who has acted in a manner contrary to the principles of equity. Pine Island Farmers Coop v. Erstad & Reimer, P.A., 636 N.W.2d 604 (Minn. App. 2001), aff'd, 649 N.W.2d 444 (Minn. 2002); Johnson v. Freberg, 178 Minn. 594, 597, 228 N.W. 159, 159-60 (1929) (“[t]he plaintiff may be denied relief where his conduct has been unconscionable by reason of a bad motive, or where the result induced by his conduct will be unconscionable either in the benefit to himself or the injury to others”); Johnson v. Johnson, 212 N.J. Super. 368, 384, 515 A.2d 255, 263 (1986) (plaintiff's breaches of fiduciary duty caused her claims to be subject to the doctrine of unclean hands which barred relief).

It is the duty of a trustee to disclose to the beneficiary fully, frankly, and without reservation all facts pertaining to the trust. In re Enger's Will, 225 Minn. 229, 30 N.W.2d 694 (1948). Respondent's failure to apprise Appellant of matters relating to the Trust before September of 2004, his failure to correct his lawyer's representations that the Trust was never funded, his failure to disclose the November 2003 assignments, and his incomplete and misleading affidavit, were all a breach of his duty of disclosure.

Jack Margolis, both before and after this litigation started, breached a number of other duties he had as Trustee of the Naomi Margolis Revocable Trust. Jack Margolis commingled Trust funds with other funds, and he converted Trust assets to his own trust through the November 2003 assignments, which undeniably were not in the best interests of the trust beneficiaries. He has retained cash distributions he has received since Naomi's death, even though there were no ongoing expenses to claim a set off against, and has continued to retain these after his lawyer committed that he would restore at least this much to the Trust. He has an admitted bias against one of the beneficiaries -- he testified under oath that he "wouldn't give her the right time of day", and told Appellant it would be a cold day in hell before his sister would ever see a dime from her mother's Estate. Margolis Dep., p. 128; T. 50. He has consistently failed to follow the spirit and explicit terms of the Trust Agreement. He failed to honor the successor trustee provision, which operates to guard against the very conflict of interest his request placed front and center before the Trial Court. The doctrine of unclean hands bars Jack Margolis' attempt to allocate nursing home and medical payments as expenses or distributions of the Trust, but

the Trial Court failed to make findings regarding his motive, his course of conduct, or his unclean hands.

II. The Trial Court Erred When It Held that Appellant Failed to Make a Sufficient Showing to Require the Trustee to Explain or Account for the Proceeds of the Norwest CD Listed in Naomi Margolis' Notes in the Amount of \$100,000, and To Restore that Amount to the Trust.

Minnesota courts have used the presumption that trust assets continue in the hands of the trustee when a beneficiary traces trust assets into the hands of the trustee and the trustee fails to prove what happened to those assets. Bogert, Trust & Trustees §923, at 451 (2d ed. 1995), citing Stein v. Kemp, 132 Minn. 44, 155 N.W. 1052 (1916); Blythe v. Kujawa, 175 Minn. 88, 220 N.W. 168 (1928); Village of Monticello v. Citizens State Bank of Monticello, 180 Minn. 418, 230 N.W. 889 (1930). These Minnesota cases have followed the black letter rule that a beneficiary makes out a prima facie case for tracing when he shows the trust assets came into the hands of the trustee, and such a showing shifts the burden to the trustee to specifically explain what happened to those assets. Bogert, supra §923, at 451. These cases establish that when a plaintiff traces the funds into the hands of the trustee or fiduciary, the funds are presumed to remain there, unless the trustee shows otherwise. Rounds, Loring A Trustee's Handbook §6.1.5.2. (2005) (all doubts are resolved against the trustee on a failure to keep adequate accounts).

The Trial Court held that Appellant had not made a sufficient showing that the Norwest CD was an asset of the Trust, as there was a lack of evidence that the asset was titled in the name of the Trust, which had the effect of relieving Respondent, who had

utterly failed to explain what happened to the CD or its proceeds, and who had actively concealed the facts regarding other Trust assets, from any responsibility.

Minnesota law is unclear on what showing needs to be made on tracing assets into the hands of a trustee. The presumption that a trustee is required to account for assets which come into his hands as trustee is an equitable concept designed to protect beneficiaries, and should not depend on direct evidence that an asset is titled in the name of the trust, which is what the Trial Court effectively held.

Courts in other jurisdictions have held that a grantor's notes which identify property to be held in the grantor's trust, executed after the creation of the trust, are sufficient evidence of intent to transfer such assets to the trust. See, e.g., Bourgeois v. Hurley, 392 N.E.2d at 1065 (a grantor trustee's exhibit which did not make reference to the trust declaration was sufficient evidence to find that the securities listed on the exhibit were part of his trust); In the Matter of the Work Family Trust, 260 Iowa 898, 907, 151 N.W.2d 490, 495 (1967) (Exhibit T-2, created five years after the trust and which identified "assets to go into the trust", was sufficient to transfer assets to the trust). A grantor who is trustee may transfer assets into a trust through a declaration of an intent to do so, regardless of whether the title to the asset is transferred. Bourgeois v. Hurley, 392 N.E.2d at 1065 (grantor/trustee may create a trust in securities by declaration, without ever engaging in the further act of transfer or reregistration); Samuel v. King, 186 Or. App. 684, 692, 64 P.3d 1206, 1210-11 (2003) (so long as the grantor actually transferred the titled assets to the trust, it was unnecessary to take further action formally transferring title of those assets to the trust).

A person's actions subsequent to executing a legal document which tend to show his or her understanding of the document's effect may be considered in determining that person's intent. Bourgeois v. Hurley, 8 Mass. App. Ct. 213, 392 N.E.2d 1061 (1979); see also, Troseth v. Troseth, 224 Minn. 35, 36, 28 N.W.2d 65 (1947) (Minnesota courts allow evidence of subsequent conduct and expressions to show a non-testate grantor's donative intent "[w]hen no other light appears to solve the problem of grantor's intent").

In the mid-1990's, Naomi Margolis told her son that the items in the notes she provided him would go to he and his sister, which could only be accomplished if placed in her Trust. The listing of the asset as a trust asset in Exhibit 16, her statements to Barry Lorberbaum, and her recognition that the social security number needed to be changed as reflected in her notes infers an agreement between Jack and Naomi Margolis regarding how the proceeds of the Norwest CD were to be treated. This and other evidence all leads to the conclusion that Naomi Margolis had an interest in the Norwest CD, and she declared it to be an asset of her Trust. This was sufficient proof to shift the burden to the Trustee, Jack Margolis, who was involved in the asset transfers, had personal knowledge, and had access to financial records, to come forward and explain what happened to this asset. Doubts are resolved against a trustee -- the Trial Court's ruling eviscerates this common law principle.

The purpose of the presumption in Minnesota law which allocates the burden to the trustee to explain what happens to trust assets is to protect beneficiaries, not obstructionist trustees. The trustee typically has either the personal knowledge or control over the record keeping to explain assets in question, and Respondent was in this position of control. As

the Minnesota Supreme Court has stated, the burden of proving that a trustee's actions conform to his duty is on the trustee:

“If * * * defendant's [trustee's] accounts are not clear and accurate, if they were negligently kept, leaving many transactions in the fog which must come of absence or ambiguity of records of old transactions, the consequent obscurity or doubt cannot operate to his advantage, but must be resolved against him.”

Smith v. Tolverson, 190 Minn. 410, 414, 252 N.W. 423, 425 (1934).

Appellant has made an adequate showing that Naomi Margolis, by her words, notes, and actions, intended and declared that a Norwest CD in the amount of \$100,000 as of 1995 or 1996 was a part of and an asset of the Trust. This is a sufficient showing to shift the burden to Jack Margolis, as Trustee of the Trust, to explain how the asset was used, whether it benefited Naomi Margolis, what occurred to the proceeds upon maturation of the CD that was held in 1995, and to specifically rebut the evidence that he had agreed to this disposition. Respondent's denial that this asset was in the Trust is not credible, given the misconduct he has engaged in with respect to Trust matters. Every single other asset listed in Naomi Margolis' notes as either in her Trust or in Jack Margolis' name has proven accurate, despite the fact that Jack Margolis at one point since her death denied that any of the other assets listed in Exhibit 16 as a part of her Trust were ever assets of her Trust.

Respondent's duty to account for the Norwest CD of \$100,000 extends “not only to the property in its original form but to any new form into which it has been changed or converted.” Rounds, Loring A Trustee's Handbook §7.2.3.1, at 379 (2005). The Trial Court erred when it failed to require Respondent to account for and restore to the Trust the

sum of \$100,000 in the way of proceeds from the Norwest CD referred to in Naomi Margolis' notes, Exhibit 16.

III. The Trial Court Erred When It Failed to Require Trustee Margolis to Make Restitution to the Trust.

A trustee has a duty to account for all trust assets, Malcolmson v. Goodhue Cty. Nat'l Bank, 198 Minn. 562, 568, 272 N.W. 157, 160 (1937), and must make restitution to the trust for all trust funds in his possession or control. Rounds, Loring A Trustee's Handbook §7.2.3.4 (2005) (discussing equitable remedy of restitution).

Appellant sought in excess of \$300,000 as restitution from Respondent. These items are set forth in Exhibits 56 and 57. These specific requests for restitution need to be evaluated separately. While Appellant's requests to surcharge Respondent involve all the items listed in Exhibits 56 and 57, two subjects are discussed separately here, and are not dependent on the use of Trust assets for nursing home expenses or the Court's findings on the Norwest CD.

Jack Margolis and the Jack Margolis Revocable Trust are obligated to restore to the Trust the sum of \$29,263.25, the sum of money received by Jack Margolis and the Jack Margolis Revocable Trust from the time of Naomi Margolis' death, which would have been the property of the Trust were it not for the November 2003 assignments which were the product of his breach of fiduciary duty. Respondent is simply not entitled to retain these funds received after her death on the basis that they were used for nursing home expenses, when that is flatly contradicted by the record. Respondent promised to restore these funds to the Trust; the Trial Court ignored his commitment. These funds were

received as a result of Respondent's conversion of Trust assets. His unclean hands bar any reimbursement by the Trust to him. The Trial Court allowed Respondent to be reimbursed from the receipt of these funds; this is devoid of any reasonable justification.

Jack Margolis and the Jack Margolis Revocable Trust are also obligated to restore to the Trust the sum of \$10,987 in the way of proceeds from the Piper Jaffray account held by the Trust which were transferred to the Jack Margolis Revocable Trust in 2001. There is no evidence at all to support the notion that these funds were used for nursing home expenses or for Naomi Margolis' benefit. The Trial Court made no finding with respect to this asset, but there is no justification to allow the Jack Margolis Revocable Trust to retain these funds.

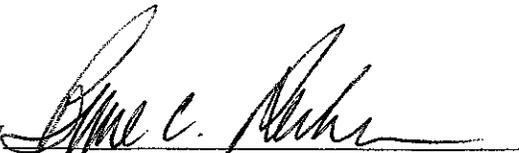
CONCLUSION

The Trial Court seemingly resolved all doubts at every turn in favor of a trustee whose conduct fell woefully short of almost every fiduciary obligation a trustee owes to a trust beneficiary. Appellant respectfully requests this Court to reverse the Trial Court's Findings of Fact and Conclusions of Law and remand the matter to the Trial Court with instructions to require Respondent to make appropriate restitution as outlined herein to the Trust.

HENSON & EFRON, P.A.

Dated: July 20, 2006.

By



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The appendix to this brief is not available for online viewing as specified in the *Minnesota Rules of Public Access to the Records of the Judicial Branch*, Rule 8, Subd. 2(e)(2) (with amendments effective July 1, 2007).