List of Legal Issues

Broken Trust:

Greed, Mismanagement & Political Manipulation at America's Largest Charitable Trust

by
Samuel P. King and Randall W. Roth

In 1884, Princess Bernice Pauahi Bishop, the last acknowledged descendant of the Hawaiian monarch Kamehameha, placed the bulk of her estate in charitable trust to establish and maintain two schools, "one for boys and one for girls … called the Kamehameha Schools." The trust corpus—known as Bishop Estate—has been described by *The New York Times* as "a feudal empire so vast that it could never be assembled in the modern world," and by *The Wall Street Journal* as "the nation's wealthiest charity." In 1997, four elders revered in the native Hawaiian community, together with a law professor from the University of Hawaii, alleged massive trust abuse by the state's most powerful people. Then, as described in a review of the Broken Trust book: "Subpoenas fly, surveillance photos are snapped, phones are bugged, tires are slashed, judges cry in court, suicide factors in. The IRS swoops in like a huge predatory bird and threatens to revoke the trust's tax-exempt status, which would cripple the schools." The following legal issues played a major role in the Bishop Estate saga:

ATTORNEY-CLIENT PRIVILEGE. Most courts do not allow trustees to use the attorney-client privilege to withhold important information about trust administration from the beneficiaries of private trusts, or from the attorney general with respect to charitable trusts. Yet the probate court ruled that the Bishop Estate trustees could use the privilege to withhold documents from Hawaii's attorney general.

CO-INVESTMENT. Bishop Estate trustees created a conflict of interests when they invested personal funds in private business deals in which they had also invested trust funds. One reason for the restriction on co-investing is that trustees will be tempted to consider their own interests when making subsequent decisions about the investment (i.e., that they will throw good money after bad for the impermissible purpose of salvaging their own private investment). Bishop Estate trustees apparently did exactly that.

COMMUNITY INTERESTS. Trustees of charitable trusts traditionally have been expected to pursue each trust's specific charitable mission, even to the detriment of other community interests. That may be changing. In 2002 the trustees of the Hershey trust voted to sell stock in the Hershey Foods Corporation for upwards of $15 billion so they could diversify trust investments and increase dramatically the money available to pursue that trust's educational mission, *but* the Pennsylvania attorney general opposed the sale, however, because of opposition from community leaders who feared that a new owner would move company headquarters and operations out of the state. Also in 2002 the new Bishop Estate trustees yielded to public pressure and withdrew from a long-standing legal battle over the trust's legal entitlement to divert mountain stream water for land-development purposes. Although this decision arguably hurt the trustees' ability to educate as many children as possible, Hawaii's attorney general and a court-appointed master supported the decision.

CONFIDENTIALITY. Fiduciaries are sometimes subject to a duty of confidentiality. Bishop Estate trustee Lindsey claimed that trustee Stender violated such a duty when he told friends, and eventually reporters, about what went on at trustee meetings. Stender claimed that Lindsey violated a duty of confidentiality when she released to the media her "confidential" report on the quality of education at Kamehameha Schools.

CONFLICT OF INTERESTS. Trustees must avoid conflicts of interest and take appropriate action when a conflict cannot be avoided completely. A Hawaii statute additionally requires that trustees seek court instructions when there is a significant conflict of interest. Bishop Estate trustees devised their own ways of dealing with conflicts. For example, trustee Peters "recused" himself as a Bishop Estate trustee just long enough to negotiate for the purchase of Bishop Estate land on behalf of the buyer.

CONTROVERSIAL ISSUES. Judges usually avoid getting personally involved in public controversies. Lawyers working for the Bishop Estate trustees looked into the possibility that Judge Samuel King acted improperly when he co-authored the Broken Trust essay. A court-appointed master later discovered that the trustees' lawyers had spent several days researching and drafting a memo entitled "Limits on freedom of federal judge regarding public statements on social issues and conclusions of law"—an action that the master later described as "chilling" and as a "wholly inappropriate" use of charitable trust funds.

COOPERATION. Co-trustees are required to work together in the best interests of the trust. Yet, Bishop Estate trustees sometimes refused to share important trust information with each other, and their working relationships became strained to a point approaching physical violence on several occasions.

***CY PRES*.** A trust's charitable mission, even one that is no longer in tune with the modern world, can be changed legally only by showing that unforeseen circumstances have made the original mission illegal, impossible, impracticable, or wasteful. The standard is less stringent when the change would affect only an administrative provision (i.e., one that is a means to an end as opposed to the end itself). Bishop Estate trustees and Hawaii's probate court sometimes have acted as if this rule does not exist. For example, although Mrs. Bishop's will directs the trustees simply to establish and maintain two schools, "one for boys and one for girls," the two schools are now combined. Furthermore, the trust also functions somewhat like a land conservancy, providing culturally and environmentally sensitive stewardship for nearly 360,000 acres of non-income-producing land. This is surely a laudatory endeavor, but Mrs. Bishop's will says nothing about preserving or protecting the environment or Hawaiian culture.

DELEGATION. Each trustee must remain responsible for, and exercise supervision and review of, all trust activities. Despite this rule, the five Bishop Estate trustees utilized a "lead-trustee" system in which individual trustees functioned like chief executives for different aspects of the trust's activities, making important decisions without first consulting with the others.

DILIGENCE. Trustees have a duty to stay informed and participate in decision making. Yet, one Bishop Estate trustee stopped attending trustee meetings because he considered the chaotic, hostile sessions to be a waste of time. He also felt that he could not influence the outcome of any issue because the other trustees regularly ignored or ridiculed what he said. Even so, his failure to attend was a serious breach of trust.

DISCIPLINARY ACTION. Lawyers are allowed to criticize judges, but there are limits. Hawaii's Supreme Court justices wrote in a newspaper commentary that the authors of the Broken Trust essay had "expressly and impliedly impugned the integrity, honesty, ethics, intelligence, qualifications, competence, and professionalism not only of the five members of the Hawaii Supreme Court as individuals, but also of the court as an institution." Although these same justices were the ultimate authority on matters of lawyer discipline in Hawaii, they never took formal action against the three lawyers who signed the Broken Trust essay.

DISCOVERY ABUSE. When engaged in litigation, it is unethical for a lawyer to make frivolous demands for documents or fail to make reasonable efforts to comply with proper requests from an opposing counsel. Yet studies suggest that some lawyers routinely seek more documents than they reasonably need (presumably to burden the opposing counsel) and go to great lengths to avoid turning over embarrassing or damning documents that the opposing party has requested. Hawaii's attorney general complained that the Bishop Estate trustees' lawyers produced an "avalanche" of unimportant documents, yet failed to produce certain key documents. She asked the court to sanction those lawyers for abusive discovery tactics, but the judge chose not to do so.

DISCRIMINATION. Mrs. Bishop's will does not limit school admission to native Hawaiians, but it does authorize the trustees to set the admissions policy and to use a portion of each year's income for "support and education of orphans, and others in indigent circumstances, giving the preference to Hawaiians of pure or part aboriginal blood." With minor exceptions, Bishop Estate trustees have always reserved admission to Kamehameha Schools for children who have Hawaiian blood. Some critics argue that applicants with a relatively high quantum of Hawaiian blood should gain admission over those with lower levels, regardless of academic ability. Others maintain that any child, regardless of race, who has been informally adopted by a Hawaiian (a cultural practice known as *hanai*), should be eligible to attend Kamehameha Schools. And then there are those who argue that "Hawaiianness" should be based on culture and interests, not blood quantum or informal membership in a Hawaiian family. A non-Hawaiian applicant, rejected by Kamehameha Schools in 2002, alleged in court that a "Hawaiians-only" admissions policy violates a nineteenth-century civil-rights statute. The trustees settled that lawsuit for $7 million while the U.S. Supreme Court was deciding whether to grant the plaintiff's petition for certiorari. Administratively, the IRS district office decided in 1999 to revoke Bishop's Estate tax-exempt status because of the "Hawaiians-only" admissions policy, but the national office reversed that decision. Since then, to reduce the risk of a 14th Amendment challenge, the trustees have rejected all direct forms of government aid.

DIVERSIFICATION. It has been said that the three most important principles for prudent investing are "diversification, diversification, and diversification," yet the Bishop Estate trustees retained most of the original estate, which was virtually all unimproved land. Depending on other factors, this could conceivably be prudent and therefore acceptable under trust law, but the Bishop trustees' periodic additions to the trust's already extensive land holdings are virtually impossible to justify under the prudent investor standard.

DUE DILIGENCE. Trustees are not allowed to make uninformed investment decisions. They must perform appropriate due diligence before investing trust funds. Bishop Estate trustees sometimes skipped that step or appeared not to take it seriously.

DUTY TO PROTECT. Each co-trustee has a duty to use reasonable care to prevent any co-trustee from committing a breach of trust and, if a breach of trust occurs, to obtain redress. Trustee Stender knew of serious breaches and tried for years to get the probate court or attorney general to take action against the other Bishop Estate trustees. He also considered filing a lawsuit, but lawyers told him it would cost at least $2 million (which would have to come out of his own pocket), and that he would probably lose (because of a perceived connection between his co-trustees and the state judiciary). Despite Stender's good-faith efforts to get others to do their job of policing the trust, he was later faulted for not filing suit against the other trustees.

FIDUCIARY DUTIES. When individuals agree to serve as trustees—which they cannot be forced to do—they automatically become subject to strict fiduciary duties, regardless of their understanding of those duties. Even so, four of the five Bishop Estate trustees declined to attend sessions on what was expected of them under trust law.

FLAWED ACCOUNTABILITY. According to the IRS and several court-appointed masters, Bishop Estate trustees treated Mrs. Bishop's estate like their personal investment club and set what arguably was a world record for breaches of trust, yet the Hawaii probate court allowed all five trustees to resign without ordering them to pay *any* surcharges, damages, or reimbursement to the trust—they were not even required to admit they had done anything wrong.

IMPARTIALITY. Trustees are required to know whether the circumstances of any particular trust require them primarily to stabilize current returns, maintain the trust estate's real value, or something else. They cannot put the interests of future generations of beneficiaries ahead of the current generation. While Kamehameha Schools was admitting only one out of every twelve applicants, Bishop Estate trustees were investing primarily for growth and secretly accumulating more than $350 million of income.

INCORPORATION. Broken Trust author Judge King suggests that it is time to convert Mrs. Bishop's trust into a not-for-profit corporation. Instead of five highly paid trustees who tend to micromanage, there would be a larger number of unpaid directors who would set policy and provide oversight to a well-paid chief executive and highly qualified staff. Because unpaid directors of not-for-profit corporations have far less legal exposure than do trustees of a trust (by statute in most states), millions of dollars could be saved on liability-insurance premiums. Also, the organization's charitable mission could evolve more easily with changing times. For example, a not-for-profit board of directors arguably could legitimately use existing resources to promote Hawaiian culture, conserve non-income-producing land, grant scholarships to Hawaiian students at schools other than Kamehameha, and expand the organization's outreach programs, without first having to establish that the charitable purpose in the will (the maintenance of two schools) is illegal, impossible, impracticable, or wasteful.

INTERIM REMOVAL. Despite reports submitted by a court-appointed master and court-appointed fact-finder that listed numerous serious, ongoing breaches of trust, the probate judge declined to take definitive action until the IRS made its presence felt, which was nearly two years after publication of the "Broken Trust" essay. When the judge finally did schedule an interim-removal hearing, a trustee who had attempted suicide requested and received a postponement so he could recuperate fully before having to protect his individual interests in court. Meanwhile, he continued to collect nearly $100,000 each month in trustee fees. The probate judge appeared to be more concerned about that trustee's due-process rights than the interests of the trust itself.

INTERMEDIATE SANCTIONS. Bishop Estate trustees spent nearly $1 million lobbying against the enactment of an intermediate-sanctions law that empowered the IRS to impose large fines on trustees for taking excessive fees. Because its enactment posed a threat only to the trustees (and provided benefits to the trust itself), the trustees' lobbying would have been a serious breach of trust, even if they had used their own money. They used trust funds.

INVESTMENT OPPORTUNITIES. Like lawyers, trustees are sometimes prohibited from benefiting personally from information gained while acting in a fiduciary capacity. After the other Bishop Estate trustees rejected a recommendation that they acquire control of Maui Land & Pineapple Company on behalf of the trust, trustee Stender pursued the opportunity for his personal account. Trustee Lindsey described this as a disloyal act even though Stender fully reimbursed the trust for the time its staff had spent while investigating the opportunity on behalf of the trust. Lindsey's attorney expressed less certainty about the propriety of Stender's actions: "Whether or not Stender engaged in a breach of his fiduciary responsibilities … is inconclusive at this time."

IRS ROLE. Historically, the IRS has played a limited role in regulating charities, deferring almost completely to local officials. But the slow-moving Bishop Estate controversy reached a sudden climax when the IRS refused to communicate with the sitting trustees and threatened to revoke the trust's tax exemption if a list of nonnegotiable demands were not met. That forced the probate court to remove the trustees and reform the trust. Was it proper for the IRS to assume such an active role? Opinions vary greatly.

LAWYER WHISTLEBLOWING. Depending on the circumstances, trust counsel may be *prohibited* from disclosing a trustee's serious misconduct (as was the rule in most states for many years), *required* to disclose any such misconduct (as is the law today in Hawaii), or *permitted* to disclose it (as is the national trend). Despite what *Broken Trust* refers to as "a world record for breaches of trust," there is no public evidence of any lawyer ever attempting to report misconduct by a Bishop Estate trustee.

MANDATORY AND PRECATORY LANGUAGE. Mrs. Bishop used mandatory and precatory language in different sections of her will. For example, she *directed* that her trustees expend annual income on the schools, publish accountings in a Honolulu newspaper, and hire only Protestants to teach at Kamehameha Schools. By comparison, she only expressed a *desire* that the trustees provide education in the common English branches, and that instruction in the higher branches always is subsidiary. Bishop Estate trustees frequently refer to Mrs. Bishop's will as "sacred," yet they regularly have deviated from not just the precatory provisions, but mandatory ones as well.

OVERSIGHT. Effective oversight is never certain. Each individual Bishop Estate trustee had a duty to monitor the actions of the other four and to take appropriate action when serious breaches of trust became evident. The Hawaii attorney general also had oversight responsibility, as did the probate court and the master the court appointed each year to review the trustees' accounts. Furthermore, the trustees' legal counsel were supposed to report serious trustee misconduct to the probate court, and Supreme Court justices arguably had on-going responsibility to monitor trustee conduct and to take action in the face of serious misconduct. Despite all this, obvious breaches of trust went unchecked for years.

PARENS PATRIAE. Beneficiaries of non-charitable trusts have legal standing to sue the trustees of their trusts. That enables such beneficiaries to hold trustees accountable. But charitable trusts technically lack beneficiaries other than the public-at-large. Rather than allow members of the public to sue trustees of charitable trusts, trust law bestows upon the attorney general of each state the power and the responsibility to represent the intended beneficiaries of every charitable trust. This concept, called *parens patriae*, has been a part of trust law for centuries. Prior to publication of the "Broken Trust" essay, however, a series of attorneys general in Hawaii took no action against Bishop Estate trustees despite obvious breaches of trust.

PERSONAL COUNSEL. When trustees retain lawyers to assist them in carrying out their fiduciary duties, it is appropriate that trust funds be used to pay the fees. Such lawyers are sometimes called trust counsel. When trustees retain lawyers to watch out for the trustees' personal interests, such lawyers are called personal counsel, and the propriety of using trust funds is less clear. In such situations it is prudent and may be required that the trustees petition the court for instructions. But Bishop Estate trustees regularly used trust funds to pay attorneys who appeared to be representing the personal interests of individual trustees, according to a court-appointed master.

POLITICAL INVOLVEMENT. Tax-exempt organizations are not supposed to involve themselves in political campaigns, yet Bishop Estate trustees systematically raised money for numerous political campaigns and paid questionable "consulting fees, retainers, and salaries" to key government officials.

PRUDENT INVESTING. Prudent investing generally requires an overall plan, due diligence prior to individual investment decisions, and regular monitoring of existing investments. Bishop Estate trustees reportedly made *ad hoc* investment decisions based on personal relationships, and without proper due diligence. For example, when Robert Rubin left Goldman Sachs to join the Clinton administration, he sold his partnership interest back to Goldman Sachs for its promissory note, and then asked Bishop Estate to guarantee that note—which was reportedly in the vicinity of $50 million. The trustees agreed to do so despite not having the expertise needed to ascertain the trust's exposure and determine an appropriate price. They also invested tens of millions of dollars in complicated oil and gas exploration deals that individual trustees could not explain during the depositions taken when they later sued the promoter.

PUBLIC CHARITY. When Mrs. Bishop wrote her will, Hawaii was an independent nation with its own tax laws. Now, however, the trust is subject to the U.S. Internal Revenue Code. Because Bishop Estate has a single benefactress, some people assume it is a private operating foundation (like the Queen Liliuokalani Trust). Bishop Estate, however, is a public charity because its charitable purpose is to operate a "school" (defined in the tax code as "an educational organization that normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on"). It is unclear to what extent the trustees can pursue other charitable purposes (e.g., outreach programs and land-conservancy activities) before the trust ceases to be classified as a school, and therefore becomes a private operating foundation, for tax purposes. If it were a private foundation, tax law would require that the trustees expend a minimum of 5% of trust value each year. Even in the years following the removal of five trustees the amount spent in pursuit of Princess Pauahi's charitable mission has never come close to 5% of trust value.

PUBLIC POLICY. Trustees arguably should not be able to enter into private contracts that limit the ability of their successors to hold them accountable for harm done to the trust, yet Bishop Estate trustees managed to accomplish that. The successor trustees chose not to seek accountability because of "insured vs. insured" provisions in $75 million of liability insurance coverage the former trustees had purchased with trust funds. The new trustees' lawyers—including some who had represented the former trustees—reportedly advised against seeking accountability or even cooperating with the attorney general's office in its effort to hold the former trustees accountable, saying that it would jeopardize the insurance coverage. The new trustees, also concerned about the personal strain and financial cost of pursuing the former trustees and the former trustees' lawyers, chose not to seek a declaratory judgment on the public-policy issue.

REGULAR ACCOUNTING. Although trustees have a duty to keep beneficiaries informed about the trust and Mrs. Bishop specifically instructed her trustees to publish an accounting in a Honolulu newspaper each year, Bishop Estate trustees were notorious for providing inadequate information. For example, they routinely used wholly owned corporations to conduct business, but they did not provide consolidated financial statements or crucial details about the corporations. They also reported trust land at values that were nearly 40 years old.

RELIANCE ON OTHERS. Trustees should not seek legal advice from lawyers who have a conflict of interests, nor should they put such a person in control of the flow of information within the organization. Yet when interim trustees replaced the ousted Bishop Estate trustees, they chose as their chief executive the person who had served for the past decade as the former trustees' top in-house lawyer, and they sought legal advice from outside counsel who had advised the former trustees.

RELIGION. In her will, Mrs. Bishop directed that trustees of her trust and teachers at Kamehameha Schools always be members of the Protestant religion. In the 1960s, a court determined that the requirement that teachers always be Protestant did not violate anti-discrimination labor laws because the school was a private, religious school. In 1994, however, the 9th Circuit ruled that the Protestants-only hiring mandate violated the law because the school had evolved into a secular institution. State Supreme Court justices claimed for years to be following the *letter* of the will (appointing, among others, a lifelong Catholic who evidently "converted" to Protestantism on the eve of his selection, and a practicing Mormon who claimed to have received Protestant baptism as an infant). Eventually, however, the justices stopped considering religion entirely. Currently the probate judge selects trustees. Presumably she ignores each candidate's religion since judges cannot ethically consider religion when making such decisions. In short, Mrs. Bishop's instructions regarding religion are no longer honored.

SECRECY. Bishop Estate employees had no choice but to sign confidentiality agreements. When a senior executive appeared poised to provide evidence of trustee misconduct to the authorities, the trustees fired him and got a court order that effectively muzzled him. He found himself unable to give the documents even to the authorities.

SEX WITH A CLIENT. Rule 1.8(j) of the Model Rules of Professional Conduct provides that "a lawyer shall not have sexual relations with a client unless a consensual sexual relationship existed between them when the client-lawyer relationship commenced." Yet a lawyer for one of Bishop Estate's wholly owned businesses reportedly had a sexual relationship with one of the trustees. Was that trustee a "client" for purposes of this rule? The answer is not clear.

SIMULTANEOUS INVESTIGATIONS. The attorney general simultaneously directed civil and criminal investigations of the Bishop Estate trustees. She instructed members of the criminal team not to communicate about the case with members of the civil team, and vice versa. The criminal team secured a series of grand jury indictments, which the civil team offered as evidence in the civil action. Eventually a judge threw out all the indictments on procedural grounds and a panel of substitute Supreme Court justices ruled that there had been prosecutorial misconduct. (All of the regular justices had recused themselves because of obvious conflicts of interest.) Trustee Wong and other members of his family unsuccessfully sued the attorney general and selected deputies for alleged civil rights violations and malicious prosecution. The action was dismissed in state court because of a "global" settlement that had abruptly ended the attorney general's civil and criminal investigations.

SPLIT-PERSONALITY TRUST. The culture at a typical charity is noticeably different than the culture at a typical business. Because Bishop Estate trustees engage extensively in business activities (directly or through profit-seeking "subsidiaries") while simultaneously operating a public charity, many people view the trust as two separate organizations with two separate cultures: a business, Bishop Estate, and a charity, Kamehameha Schools. A succession of trade names suggests an evolution of self-identity (i.e., what for many years was officially known as Bishop Estate eventually became Bishop Estate/Kamehameha Schools, then Kamehameha Schools/Bishop Estate, and finally Kamehameha Schools). Some observers call this frequent rebranding window dressing, and contend that the trustees should become a true charity with only passive-investment assets in its endowment. They further contend that the trust's split personality as part business/part charity renders it less effective than it otherwise could be as either a business or a charity.

STANDING. There is a national trend toward granting legal standing to groups that have a special interest in a particular charitable trust when the state attorney general chooses not to take action despite indications of serious abuse. When it became clear that the system of oversight in Hawaii had broken down and that no one with legal standing was taking steps to hold the Bishop Estate trustees accountable, a group of Kamehameha Schools alumni, parents, students, and teachers asked for standing. Hawaii's attorney general joined with the Bishop Estate trustees in successfully opposing those efforts.

TAX-EXEMPT STATUS. Change came quickly to Bishop Estate after the IRS threatened to revoke the trust's tax-exempt status. The sitting trustees had apparently violated every condition of IRC section 501(c)(3) status: *private inurement* (excessive compensation and inappropriate side benefits), *private benefit* (sweetheart deals for friends and relatives), *commerciality* (overemphasis on the business side of trust activities), *failure to pursue the charitable mission* (less than 1% of estimated value expended on Kamehameha Schools each year), *involvement in political campaigns* (illegal financial assistance to, and direct involvement in, the campaigns of favored candidates), and *self-serving lobbying activities* (more than a million dollars of trust funds secretly spent lobbying against federal and state legislation that would limit how much the trustees could pay themselves in compensation).

TRIAL PUBLICITY. Legal ethics sometimes limit what a lawyer can say to the media about matters that are being litigated. With this in mind, lawyers for the Bishop Estate trustees complained in open court that media outlets were quoting one of the authors of the Broken Trust essay on how the judge should rule on specific issues, saying that it was having an inappropriate influence on the court. Perhaps because the ethical rule applied only to lawyers who were participating directly in the litigation, however, the probate judge took no action.

TRUST COUNSEL. Some of the lawyers in the Bishop Estate controversy said they were representing "the trust," took orders from the three-trustee majority faction, and reportedly did not communicate fully with the other two trustees. Yet trusts are traditionally viewed as relationships between trustees and beneficiaries, not as separate entities. Under this view, the minority trustees continued to be "clients." Lawyers cannot withhold relevant information from their own clients.

TRUSTEE SELECTION. Settlors should consider the best way to select future trustees, especially if they expect the trust to last many years into the future. Mrs. Bishop directed that Supreme Court justices select all her future trustees. At the time, Hawaii was an independent nation. More than a century later, state justices were still selecting trustees, supposedly in their non-official capacity as ordinary citizens (because the Supreme Court had only appellate jurisdiction over probate matters). By the 1990s, critics concluded that the justices were selecting trustees on the basis of political payback, with no apparent concern for the trust's intended beneficiaries. A few months after publication of the Broken Trust essay, the justices announced that they would stop selecting trustees, citing a "climate of public cynicism." Currently the probate judge chooses all Bishop Estate trustees. Hawaii's last monarch, Queen Liliuokalani, empowered her trustees to select their own successors. While one can easily envision problems with self-perpetuating boards, that approach has worked well for the Queen Liliuokalani Trust. As for the Bishop Estate, critics now question whether a single probate judge can reasonably be expected to withstand the intense political pressures that appear to have controlled the actions of five Supreme Court justices.

UNDIVIDED LOYALTY. Trustees must act at all times solely in the beneficiaries' best interests, and in so doing, they must meet an unusually high standard of care and conduct. The duty of undivided loyalty includes an absolute prohibition against self-dealing—which Bishop trustees breached when they refused to step aside in the face of an IRS demand to do so in order to save the trust's tax-exempt status. The trustees called this requirement "extortion." It is easy to see how such a threat could be used maliciously, but whether it was fair to the trustees did not matter. The threat to the trust was real, and so the trustees were duty-bound to step down.

UNITRUST. According to Mrs. Bishop's will, as interpreted by the Hawaii Supreme Court, the trustees were supposed to expend all trust income annually on Kamehameha Schools. This arguably meant that they had a duty to invest assets in such a way as to generate a reasonable amount of annual income. Yet for years the trustees invested primarily for growth and never spent as much as 1% of trust's current value. Now, at the

IRS's insistence, the trustees annually expend approximately 4% of the trust's *endowment* value, which excludes nearly 360,000 acres of non-income-producing land).

UNPRODUCTIVE ASSETS. Trustees have a duty to make the trust estate productive. Bishop Estate trustees, however, own nearly 360,000 acres of non-income-producing land (including 63 miles of valuable shoreline), worth billions of dollars. They do not list these parcels of land as investments; instead, they call them "program assets" that are being held indefinitely "for educational purposes." Bernice Pauahi Bishop expressed a desire that the trustees not sell her land "unless in their opinion a sale may be necessary for the establishment or maintenance of said schools, or for the best for the best interests of my estate." Critics contend that the trustees should sell the land so they can educate more Hawaiian children, and that the trustees have a duty to do so.

WAIVER OF ATTORNEY-CLIENT PRIVILEGE. The Hawaii Supreme Court threw out criminal indictments against the former Bishop Estate trustees after ruling that grand-jury testimony had violated the attorney-client privilege. The new trustees had waived the privilege, but the justices said the question of who could waive the privilege (i.e., the former or current trustees) was an unresolved question that was best left for another day. Cases in other jurisdictions are mixed.

WASTE. A court-appointed master concluded that the Bishop Estate trustees had wasted trust funds on lawyers who represented the trustees' personal interests. The master recommended that the successor trustees seek disgorgement of millions of dollars in fees already paid to certain lawyers. Instead, the successor trustees sought a "second opinion" from a law firm that advised the successor trustees not to attempt to recover any of the fees in question, and indicated that it would be okay for the trustees to rehire many of the lawyers who had served the former trustees for many years. Critics contended that the $1 million cost of the "second opinion" was itself a waste of trust resources.

WILL CONSTRUCTION. Mrs. Bishop's will gives her trustees discretion "to devote a portion of each year's income to the support and education of orphans, and others in indigent circumstances." It is tempting to view this as a second charitable mission, one that is separate and apart from the primary mission of running Kamehameha Schools. But Hawaii's Territorial Supreme Court ruled in 1910 that support and education, as used in Mrs. Bishop's will, must be provided at the Kamehameha Schools: "The construction contended for by the [attorney general] that the support and education contemplated was to be furnished elsewhere than at the schools and that support can be furnished independently of education would require undue straining of the language used…. In our opinion the clause under consideration refers to support and education at the Kamehameha Schools only and not to support independently of education."

Additional information about the book can be found at www.brokentrustbook.com