VIRGINIA: IN THE CIRCUIT COURT FOR THE CITY OF NORFOLK

VIRGINIA STATE BAR EX REL
FIRST DISTRICT COMMITTEE
VSB Docket No. 18-010-110420

v. Case No. CL19-5110

PHILIP R. FARTHING

CONSENT TO REVOCATION ORDER

On January 16, 2020 came Philip R. Farthing by counsel Paul D. Georgiadis and tendered an Affidavit Declaring Consent to Revocation of his license to practice law in the Commonwealth of Virginia pursuant to Part VI, Section IV, Paragraph 13-28 of the Rules of Court (hereinafter "Affidavit"). By tendering his Affidavit at a time when allegations of Misconduct are pending, the nature of which are specifically set forth in the attached Affidavit, Respondent acknowledges that the material facts upon which the allegations of Misconduct are pending are true. The Panel having considered the Affidavit, and Bar Counsel having no objection, the Panel accepts the Consent to Revocation. Upon consideration whereof, it is therefore ordered that Philip R. Farthing's license to practice law in the Commonwealth of Virginia be and the same hereby is REVOKED, and that the name of Philip R. Farthing be stricken from the Roll of Attorneys of this Commonwealth.

It is further ORDERED that an attested copy of this order be mailed to: Paul D. Georgiadis, counsel for Respondent, at Law Office of Paul D. Georgiadis, PLC 2819 North Parham Road, Suite 110, Richmond, Virginia 23294-4425, M. Brent Saunders, Senior Assistant Bar Counsel, Virginia State Bar, 1111 East Main Street, Suite 700, Richmond, Virginia 23219-0026; and the Clerk of the Disciplinary System, Virginia State Bar, 1111 East

Main Street, Suite 700, Richmond, Virginia 23219-0026.

This case is hereby closed and stricken from the active docket of the court.

ENTERED: January 21, 2020

The Honorable Victoria A.B. Willis
Chief Judge

I ASK FOR THIS:

Paul D. Georgiadis
VSB No. 26340
Law Office of Paul D. Georgiadis, PLC
2819 North Parham Road, Suite 110
Richmond, Virginia 23294-4425
804.270.1154
PDGLex@PDGLex.com

SEEN AND AGREED:

Shelley L. Spalding
Assistant Bar Counsel
VSB No. 47112
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VIRGINIA: IN THE CIRCUIT COURT FOR THE CITY OF NORFOLK

VIRGINIA STATE BAR EX REL
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v. Case No. CL19-5110

PHILIP R. FARTHING

AFFIDAVIT DECLARING CONSENT TO REVOCATION

Philip R. Farthing, after being duly sworn, states as follows:

1. I was licensed to practice law in the Commonwealth of Virginia on February 9, 1973;

2. I submit this Affidavit Declaring Consent to Revocation pursuant to the applicsble provisions of Rule of Court, Part 6, Section IV, Paragraph 13-28;

3. My consent to revocation is freely and voluntarily rendered, I am not being subjected to coercion or duress, and I am fully aware of the implications of consenting to the revocation of my license to practice law in the Commonwealth of Virginia;

4. I am aware there is currently pending a complaint, an investigation into, or a proceeding involving, allegations of misconduct, the docket number for which is set forth above, the specific nature of which is:

   a. On August 8, 1996, Ivan Higgerson made the Ivan Higgerson Revocable Trust Agreement appointing me as trustee. The Revocable Trust required that the trust corpus be divided into two trusts upon Mr. Higgerson's death—The Marital Trust and The Family Trust. In 1998, Mr. Higgerson appointed me as trustee for the Irrevocable Life Insurance Trust Agreement of Ivan Higgerson. These trusts (collectively the "Trusts") were for the benefit of Mr. Higgerson's wife, Edith Higgerson, and family. In 1999, Mr. Higgerson died.

b. On December 2, 2014, Ms. Higgenson filed suit against me and my law firm in the Circuit Court of the City of Chesapeake. The suit alleged, *inter alia*, breach of fiduciaries duties. On May 6, 2015, the court replaced me as trustee for the Trusts with my consent.

c. On February 2, 2016, Ms. Higgerson died. On March 25, 2016, the co-executors of Ms. Higgerson's estate, along with the other family beneficiaries of the Trusts, filed an amended complaint against me.

d. A bench trial was held on November 7-8, 2016 before The Honorable John W. Brown. Final argument was held on November 21, 2016 and additional evidence was received on April 3, 2017.

e. On June 20, 2017, Judge Brown issued a letter opinion finding that I was liable to the plaintiffs in the amount of $1,382,653.00 for breach of my fiduciary duties and in the amount of $770,471.33 for unreasonable trustee fees. Judge Brown's letter opinion is attached hereto as Exhibit A and incorporated herein by reference. I strongly contested the Court's findings

f. On July 20, 2017 Judge Brown entered an Amended Final Judgment Order, attached hereto as Exhibit B and incorporated herein by reference.

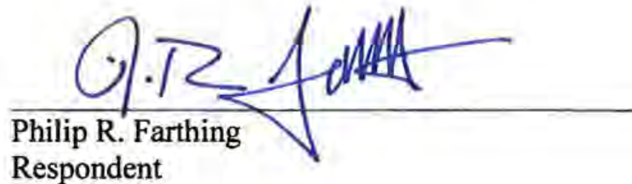
g. On March 13, 2018, the Supreme Court of Virginia issued an order finding ~~no reversible error~~ ~~in~~ there were no grounds for an appeal of Judge Brown's judgment and refusing my petition for appeal.

h. On July 7, 2016, I transferred ~~his~~ my membership class with the Virginia State Bar from active to retired. Despite not being authorized to practice law, I practiced law from April through December 2017.

5. I acknowledge that ~~the~~ that the Chesapeake Circuit Court ruled against me and that the opinion of the trial court findings are true and I acknowledge the material facts upon which the allegations of misconduct are predicated are true; and

6. I submit this Affidavit and consent to the revocation of my license to practice law in the Commonwealth of Virginia because I know that if the disciplinary proceedings based on the said alleged misconduct were prosecuted to a conclusion, I could not successfully defend against the RPC 1.5(a) and 5.5(c) violations.

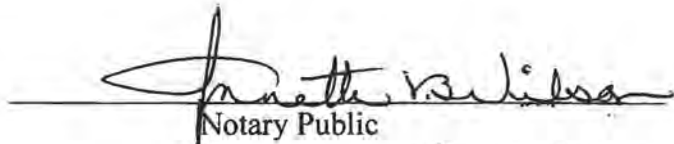
Executed and dated on January 13, 2020.



Philip R. Farthing
Respondent

COMMONWEALTH OF VIRGINIA
CITY/COUNTY OF City of Norfolk, to wit:

The foregoing Affidavit Declaring Consent to Revocation was subscribed and sworn to before me by Philip R. Farthing on January 13th 2020



Notary Public

My Commission expires: June 30, 2020

FIRST JUDICIAL CIRCUIT
OF VIRGINIA

[illegible]

[illegible]

June 20, 2017

Gregory S. Larsen, Esquire
Roy, Larsen, Carnes & Romm, P.C.
109A Wimbledon Square
Chesapeake, VA 23325

James A. Cales III, Esquire
Jonathan R. Hyslop, Esquire
Furniss, Davis, Rashkind & Saunders, P.C.
Smithfield Bldg., Suite 341B
6160 Kempsville Circle
Norfolk, VA 23502

Re: Ivan L. Higgerson, Sr. & Sandra H. Butt as Co-Executors of the Estate of Edith A. Higgerson, Deceased; Ivan L. Higgerson, Sr. & Sandra H. Butt, Individually, & Ivan L. Higgerson, Jr., Christie L. Fowler, Tara L. Greife, & Leslie O. Eshelman; and Elizabeth Mottu Allen, Esq., as the Trustee of the Ivan Higgerson Revocable Trust Agreement, the Ivan Higgerson Marital Trust, the Ivan Higgerson Family Trust, and the Irrevocable Life Insurance Trust Agreement of Ivan Higgerson v. Phillip R. Farthing, Esq., as the Former Trustee of the Ivan Higgerson Revocable Trust Agreement, the Ivan Higgerson Marital Trust, the Ivan Higgerson Family Trust, and the Irrevocable Life Insurance Trust Agreement of Ivan Higgerson, Phillip R. Farthing, P.C., and Phillip R. Farthing in his individual capacity
Civil No.: CL14-2929

Dear Counsel:

This matter came before the Court for a bench trial on November 7-8, 2016, for final argument on November 21, 2016, and for the formal admission of an additional piece of the plaintiff's evidence on April 3, 2017. Following a review of the transcripts filed in

VSB Exhibit

A

this matter, and the extensive exhibits submitted by the parties, the Court is prepared to rule.

BACKGROUND & ISSUES

The gravamen of the complaint in this case is the defendant's alleged failure to properly act in his fiduciary capacity as trustee for various trusts established by Ivan Higgerson: the Ivan Higgerson Revocable Trust Agreement, the Ivan Higgerson Marital Trust, the Ivan Higgerson Family Trust, and the Irrevocable Life Insurance Trust Agreement of Ivan Higgerson. The amended complaint alleges, among other things, breaches of fiduciary duties stemming from excessive fees, day trading, margin trading, failure to make distributions, and failure to make proper accountings to the trust beneficiaries.

In the trial of this case, the evidence appertained to the above allegations, and various questions were raised by the parties, the answers to which, it was said, would provide the basis for a verdict. Among them were the following questions:

(1) Did the defendant violate the prudent investor rule of Code § 64.2-780 et seq., (particularly Code § 64.2-782(A)) by:
   a. trading stock in such a way as to be designated a day trader and/or
   b. purchasing stock on margin?

   Did these actions violate the statutory requirement to exercise reasonable care, skill, and caution in the handling of the trust assets? If they did, what were the damages related to any breach?

(2) Did the defendant claim and receive fees in excess of what would be reasonable compensation as allowed under the trust instruments and the law?
   If so, what were the damages related to those alleged breaches of the duties of loyalty and care?

(3) Could the defendant charge a fee based on a percentage of the passive holding value of Higgerson-Buchanan stock that comprised approximately 32% of the company and for which the defendant had no managerial or operational responsibility?

(4) With regard to the separate portfolio of stocks, is it permissible for the defendant to charge fees for his time "day trading," which for one year showed him engaging in over 2,500 sales per calendar year?

(5) Did the defendant breach his duties of care and loyalty in not keeping his sole beneficiary apprised of the activities of the trust through a report/accounting that clearly sets forth his actions with respect to the trust assets? Specifically, (a) does he have a duty to inform his beneficiary that Charles Schwab made a

determination that he was a "pattern day trader;" and (b) does he have a duty to inform his beneficiary that he was buying stocks on margin and had incurred debt due to that activity?

(6) Does the defendant have a duty to clearly show how he earned the claimed fees that he withdrew from the trust without prior notice? Does he have a duty to clearly and periodically set forth the gains and losses in one section of the reports/accountings for review by the beneficiary? Does he have a duty to report (anywhere in the report) that he has, by his trading stock on margin, incurred debt for the trust? If any of these constitute breaches, what damages were the proximate result thereof?

(7) Were the assets of the trust properly valued by the defendant? Did the defendant inappropriately utilize 100% of the value of the Higgerson-Buchanan stock as the value of the 32% share, or did he properly assess the 32% share of the Higgerson-Buchanan stock?

These issues are considered in light of the amended complaint, which sets forth the following counts: (1) breach of fiduciary duty; (2) conversion; and (3) unjust enrichment.

ANALYSIS

Count I: Breach of Fiduciary Duty

Code § 64.2-764(A) mandates that "[a] trustee shall administer the trust solely in the interests of the beneficiaries." Accordingly, Code § 64.2-763 provides:

> Upon acceptance of a trusteeship, the trustee shall administer the trust and invest trust assets in good faith, in accordance with its terms and purposes and the interests of the beneficiaries, and in accordance with this chapter. In administering, managing and investing trust assets, the trustee shall comply with the provisions of the Uniform Prudent Investor Act (§ 64.2-780 et seq.) and the Uniform Principal and Income Act (§ 64.2-1000 et seq.).

"Except as otherwise provided . . . a trustee who invests and manages trust assets owes a duty to the beneficiaries of the trust to comply with the prudent investor rule set forth in this article." Code § 64.2-781(A).

The standard of care under the prudent investor rule is set forth in Code § 64.2-782:

> A. A trustee shall invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and

other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution.

B. A trustee's investment and management decisions respecting individual assets shall be evaluated not in isolation but in the context of the trust portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust.

C. Among circumstances that a trustee shall consider in investing and managing trust assets are such of the following as are relevant to the trust or its beneficiaries:

1. General economic conditions;

2. The possible effect of inflation or deflation;

3. The expected tax consequences of investment decisions or strategies;

4. The role that each investment or course of action plays within the overall trust portfolio, which may include financial assets, interests in closely held enterprises, tangible and intangible personal property, and real property;

5. The expected total return from income and the appreciation of capital;

6. Other resources of the beneficiaries;

7. Needs for liquidity, regularity of income, and preservation or appreciation of capital; and

8. An asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries.

D. A trustee shall make a reasonable effort to verify facts relevant to the investment and management of trust assets.

E. A trustee may invest in any kind of property or type of investment consistent with the standards of this article.

F. A trustee who has special skills or expertise, or is named trustee in reliance upon the trustee's representation that the trustee has special skills or expertise, has a duty to use those special skills or expertise.

G. A trustee may hold any policies of life insurance acquired by gift or pursuant to an express permission or direction in the governing instrument including an authority granted by subdivision B 19 of § 64.2-105 with no duty or need to (i) determine whether any such policy is or remains a proper investment, (ii) dispose of such policy in order to diversify the investments of the trust, or (iii) exercise policy options under any such contract not

essential to the continuation of the life insurance provided by such contract. However, apart from these specific authorities, this subsection is not intended and shall not be construed to affect the application of the standard of judgment and care as set forth in this section. This subsection shall apply to all trusts, regardless of when established.

Prudent Investment

The Court now addresses in turn whether the defendant breached his fiduciary duties and specifically violated the prudent investor rule of Code § 64.2-780, et seq. by: (1) acting as a day trader, as determined by the trust's brokerage; and/or (2) buying stock on margin. If the defendant's conduct violated the rule, the Court must accordingly determine the damages related to such breach.

The plaintiff alleges that the defendant breached the applicable standard of care by engaging in margin trades and conducting excessive trades so as to constitute a pattern of day trading, as well as lying to Charles Schwab regarding whether he possessed express authorization to conduct margin trades.

> A margin account is a means by which an investor borrows money to buy stock. The collateral for the loan is the stock in the investor's brokerage account. The lender, which is the brokerage firm, charges interest on the loan and, under certain conditions, can call the loan due. When called due, the investor has so many days to "settle" the account; that is, to repay the loan

In re Trust of Somma, 49 Va. Cir. 213, 215-16 (Richmond City 1999); *see* Black's Law Dictionary 19, 986 (8th ed. 2004) (defining "margin account," "margin," and "margin transaction," respectively).

Day trading is defined as: "The act or practice of buying and selling stock shares or other securities on the same day, [especially] over the Internet, [usually] for the purpose of making a quick profit on the difference between the buying price and the selling price." Black's Law Dictionary 1534; *see In re Trust of Somma*, 49 Va. Cir. at 214 ("The accounting shows more than 600 separate investment transactions during the accounting period. Many transactions involving a single investment occurred on the same day or within one or two days of each other. Such transactions are known as 'day trading.'").

In the absence of mandatory authority, this Court does not find that margin trading and day trading are *per se* violative of the duty of prudent investment. *Cf.* Robert J. Aalberts & Percy S. Poon, *Derivatives and the Modern Prudent Investor Rule: Too Risky or Too Necessary?*, 67 Ohio St. L.J. 525, 541 (2006) (citing Bevis Longstreth, *Modern Investment Management and the Prudent Man Rule* 134 (1986)) (arguing that although

some derivatives are designed to mitigate risk, they have gained a historical negative reputation as "imprudent per se" due to their tendency to be traded on margin). Indeed, the Restatement (Second) of Trusts considered the purchase of securities on margin to be presumptively improper for a fiduciary, although the Restatement (Third) is more nuanced in its approach. *Compare* Restatement (Second) of Trusts § 227 cmts. f, m (1959), *with* Restatement (Third) of Trusts § 227 (1992). When defense counsel read section 90 of the Restatement (Third) of Trusts,[3] addressing the general standard of prudent investment, to plaintiff's expert in trusts and estates, Robert C. Miller, an attorney with an L.L.M. in tax law, he responded that while that may be the pronouncement, it all must be taken in context and applied to a particular set of facts and circumstances. (*See* Tr. of 11/8/16 at 19. ("[I]f you took that specific statement right there, under some circumstances it could be correct. There's no question about it. [Here w]e're talking about a trust where the whole thing was put into this kind of strategy. Not 10 percent. Not 5 percent.").)

The plaintiffs' second expert, Beth Patterson, possesses an M.B.A., and was accepted by the defendant as an expert in the field of financial planning and investments. She provided a clear and understandable circumstance under which it might be appropriate for a fiduciary to borrow money on margin — where it is necessary to provide funds to the beneficiary and where the market has dropped precipitously, and the investor does not wish to sell stock to meet that need. (Tr. of 11/8/16 at 174-75.)

Indeed, as reflected by the evidence presented, the defendant's persistent margin and day trading constituted not 10% or even 20% of the portfolio: 100% of the non-Higgerson Buchanan stock was at risk. Further, the defendant was not truthful when he advised Charles Schwab on their written form as authorization that he had "specific authority" to trade on margin. Additionally, although the defendant still claims not to be a day trader, he was identified as such by an algorithm of Charles Schwab. (*See* Plaintiff's Exhibit 14 ("Important notice: You've been classified as a pattern day trader.").) Yet even after

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[3]

> The usual emphasis on long-term investing, however, does not prevent the use of active management strategies, nor does it necessarily preclude a trust investment strategy that makes competent use of investments or techniques that are often characterized as risky or speculative. Such investments, for example, real estate and venture capital, or techniques, for example, borrowing and options or future transactions, are not prohibited as long as they are employed in a manner that is *prudently designed to reduce the overall risk of the trust portfolio or to allow the trust in appropriate circumstances to achieve a higher return expectation without a disproportionate increase in the overall level of portfolio risk*. Furthermore, although it is ordinarily helpful in justifying the reasonableness of a trustee's conduct to show that an investment or strategy is widely used by trustees in comparable trust situations, the absence of such use does not render imprudent the informed, careful use of unconventional assets or techniques.

(Tr. of 11/8/17 at 9 (emphasis added).)

those faults, he compounded his breach of the duties of loyalty and care to Ms. Higginson, an 89-year-old sole beneficiary, by failing to reflect in the accountings that he was day trading, per Schwab, that he traded on margin and incurred debt for the estate by such trading, or that he made over 2,500 trades during the calendar year 2013, turning over the value of the portfolio approximately 35 times in that year. (*See* Tr. of 11/7/16 at 41; Tr. of 11/8/16 at 59-65.)

Under the circumstances of this case, the Court finds that these actions are such that they constitute breaches of the defendant's fiduciary duty to act as a prudent investor. *See generally In re Trust of Sosna*, 49 Va. Cir. 213 (trustee violated his fiduciary duty to exercise the care of a prudent investor by day trading); Restatement (Second) of Trusts § 227 cmt. f ("Unless it is otherwise provided by the terms of the trust, the following are not proper trust investments: 1. purchase of securities for purposes of speculation, for example, purchase of shares of stock on margin . . . .").

Damages

The loss calculations of plaintiff's expert Beth Patterson were based on benchmarks — the S&P 500 for equity stocks and Deutsche Bank USA bonds for fixed income and cash in a 75/25% split — for the investment community, of which the defendant was a part,[7] based on his actions. (*See* Tr. of 11/08/16 at 69-70, 98, 101-02, 107.) While the Court recognizes that the benchmarks employed by Ms. Patterson are not the exclusive means to determine whether a fiduciary's investments were reasonable, they do represent a discrete method. *See Hart v. Hart*, 27 Va. App. 46, 64-66 & n.4 (1998) (allowing use of the *Brandenburg* formula for valuation of hybrid property, but stating "we do not intend to imply that this is the only acceptable method"). All cases such as the one at bar are fact-specific and as no alternative benchmarks were offered by the defendant, the Court finds these benchmarks to be reasonable.

Accordingly, the Court finds credible the testimony of plaintiff's expert Patterson, and accepts Plaintiff's Exhibits 19-23 as accurately reflecting the damages, as calculated by her office, incurred by the trusts as a result of the defendant's day and margin trading (damages in the amount of $1,382,653). (*See* Tr. of 11/8/16 at 66, 102.) During the three-month period from August to October 2011, the trusts incurred total losses, as compared to Ms. Patterson's investment standard, of $1,614,668, wherein the defendant's day trading and extensive use of margin exacerbated losses.[8] (Tr. of 11/8/16 at 74-75; Plaintiff's Ex. 20-22.) The Court notes that after the aforementioned drop, through the

[7] The defendant cannot escape liability by claiming that he was just an everyday investor; nor can he claim any special circumstances to warrant his actions — the trusts at issue were, in the words of Mr. Miller, "plain vanilla," and required no special handling.

[8] This period includes a 32% loss in portfolio value for the month of August, and a 40% for the month of September. (*Id.* at 75.)

end of the defendant's tenure as the trusts' fiduciary, his performance generally tracked the market, as demonstrated in Plaintiff's Exhibits 17-19,[4] thus reducing the attributable losses to the testified $1,382,653.

The Court recognizes the argument made by the defendant that Code § 64.2-787 requires any compliance review of the investment activities of the trustee to be determined in light of the facts and circumstances existing at the time of the trustee's decision or action, and not in hindsight. Ms. Patterson, while admitting that she did not know the facts and circumstances of each trade made by the defendant (because she "was not there"), gave him the "benefit of the doubt" regarding nearly all of his actions and the timing thereof, and examined his investments "over a complete market cycle." (Tr. of 11/8/16 at 98-99, 108-09, 169-73.) However, it was her testimony that the rampant day trading of the defendant and his pledging of 100% of the trust assets (excluding Higginson-Buchanan stock) to purchase stock on margin was not reasonable, resulting in the precipitous drop in the value of the trusts during the aforementioned three-month period. (See Plaintiff's Ex. 17-19.) That conclusion is further supported by the fact that almost two years later, in the calendar year 2013, the defendant's activities peaked, when he made over 2,500 trades and turned over the portfolio more than 55 times.

The defendant, an attorney by training, had some experience in an accounting office years ago. (Tr. of 11/7/16 at 73.) However, his only source of training for investing funds in the stock market was his on-the-job experience as gained by reading publications. (Tr. of 11/7/16 at 77-78.) While the defendant testified that he had other trusts for which he likewise invested, his actions in the instant case were not justified by any circumstances that he enumerated at trial; his stated goal was making sufficient money to fund his sole beneficiary, despite admitting that he did not know what other income she received or from what source, a violation of Code § 64.2-782(C)(6). Knowledge of the beneficiary's other income, if any, is a potential circumstance that may have dissuaded the defendant from his rampant day trading as well as pledging 100% of the stock account to purchase additional stock on margin. Because Mr. Farthing is an attorney, he escapes those regulations that would require him to meet certain criteria and be answerable to entities such as the Securities and Exchange Commission. (See Tr. of 11/8/16 at 61.) Without limitation, the defendant was left to invest as often as he wished, and whenever he wished, even when it meant pledging 100% of the available stock assets to trade additional stock on margin. This was not a case of a specific circumstance or requirement of the trust that forced the defendant to take certain steps in order to satisfy express mandates; it is simply a matter of the defendant betting someone else's funds by day trading and buying stock on margin in order to generate returns to support the $1,657,000 in fees he removed from the trusts. Compounding these errors, the defendant failed to

[4] Defense counsel waived objection to these charts. (See Tr. of 11/8/16 at 80, 83, 88-89, 91, 94, 102-03.)

apprise the beneficiary that he was trading stock on margin and incurring debt by trading on margin. Nor did he ever advise her of the method of calculating his fees or his rate of pay, a clear violation of Code § 64.2-775(B)(4). Regarding the day trading, despite the facts brought out at trial, the defendant denied that he was a day trader, and claimed that he did not lie to Charles Schwab about possessing "specific authority" to trade or purchase stock on margin, because the operative statutes gave him the right to borrow money on behalf of the trust. It should be noted that in any of his explanations, the defendant never stated what role his day trading and margin purchases played in his overall investment strategy. *See* Code § 64.2-782(C)(4). The magnitude of the defendant's day trading is best summarized by Ms. Patterson: "In 2011, the average portfolio value was $265,789 in the revocable trust, the marital trust. During this time period, there were sales of $14,464,556. Just let that sink in for a moment. [$]265,789 average value, and just the sales side was [$]14,464,000. In 2012, the proceeds were [$]17,526,000. . . . In 2013, there [were] [$]19,958,399 in sales. The purchases were over [$]20 million." (Tr. of 11/8/16 at 62-64.)

The Court therefore determines that the defendant's unauthorized day trading and purchases of stock on margin were reckless, contrary to the prudent investor rule, and constituted breaches of his fiduciary duties, and accepts Plaintiff's Exhibits 20-23, specifically focusing on the August – September 2011 period, as an accurate reflection of the damages incurred by the trusts in the amount of $1,382,653. (*See* Tr. of 11/8/16 at 66; Plaintiff's Ex. 23.)

Reasonable Compensation

This analysis must begin with any definition of "reasonable compensation" found in the trust instruments themselves. Unfortunately, as illustrated below, the terms, although employed, are undefined in the relevant trust documents.

The Revocable Trust Agreement of Ivan Higgerson states: "For his services[,] the Trustee or his successors, shall receive reasonable compensation at the time such compensation shall become due and payable, plus reimbursement of all expenses. Such compensation of the Trustee may vary from time to time." (Plaintiff's Ex. 1 at 12.)

The Irrevocable Life Insurance Trust Agreement of Ivan Higgerson likewise provides: "For his services[,] the Trustee or his successors, shall receive reasonable compensation at the time such compensation shall become due and payable, plus reimbursement of all expenses. . . . Reasonable compensation shall be the compensation normally charged by the Trustee at the time the services are rendered, and such compensation may vary from time to time." (Plaintiff's Ex. 2 at 13-14.)

The definition of "reasonable compensation" applicable to the instant case likewise cannot be found in the Code of Virginia, although the concept is referenced in various

provisions of Title 64.2. However, the Supreme Court of Virginia has made clear that while there is no set formula, the facts of each case provide the basis for any determination of reasonable compensation. *See, e.g., Virginia Trust Co. v. Evans*, 193 Va. 425, 433 (1952) ("The allowance or refusal of compensation rests in the sound discretion of the court under the circumstances of each case."). In *Trotman v. Trotman*, 148 Va. 860 (1927), the Court stated that "reasonable compensation" is "to be measured by the conscience of the trial court." *Id.* at 868.

The Court must address whether the defendant claimed and received fees in excess of what would be reasonable compensation as allowed under the trust instruments and the circumstances of the case. Part of that analysis requires the Court to decide whether it is permissible for the defendant to charge a percentage fee on the passive holding (as a minority shareholder) of the Higginson-Buchanan stock, approximately 32% of the company, over which the defendant had no managerial or operational responsibility. If it is found that the defendant impermissibly awarded himself fees in excess of what is reasonable, the Court must determine the damages resulting therefrom.

The defendant claims that he used a fee schedule he developed at his former firm, years before he became the fiduciary and this action arose. Indeed, he admitted using the same schedule in assessing fees for these trusts while he was with his previous firm. Those annual fees, for the same trusts, however, were $7,198.50, $27,557.00, $34,486.35, $35,967.25, $16,362.35, $15,845.50, and $25,020.50 in the years 2000 through 2006, respectively, far less than the amounts assessed by the defendant after he left the firm and managed the trusts with his own firm (which fees ranged from $96,906.00 to $146,077.04 per year), as shown at trial. The defendant, for example, paid himself fees from all trusts of $113,287.50 in 2010, the same year that he cut the beneficiary's annual income from $86,000 to $0. Additionally, his "reporting" of these fees in the reports filed at the end of that year — paragraph-long descriptions of work done, did not mention the amounts he was charging, or the method he was using in arriving at those fees. Mr. Miller, plaintiff's expert, after reading all of the defendant's reports, could not determine the defendant's method of assessing fees; his best guess, however, was that the defendant was utilizing an hourly rate. (Tr. of 11/7/16 at 209.)

In this case, much of the testimony from both experts addressed the Guidelines for Fiduciary Compensation ("Guidelines"), approved by the Commissioners of Accounts in Virginia and the 2005 Judicial Council of Virginia. While this was not a case that came before any Commissioner of Accounts, chapter 22 of the Manual for Commissioners of Accounts (5th ed. 2014) ("Manual") addresses those Guidelines:

> The introduction to the Guidelines states, in part, "[t]he guidelines are not intended as a substitute for the analysis the Commissioner must do to determine the statutory 'reasonable compensation' in each case." For this reason, the material formerly included in the numbered paragraphs below is

> continued. The Guidelines are not law. The *law* controlling fiduciary compensation is contained in the statutes (primarily Va. Code § 64.2-1208) and in court decisions; it remains the same and continues to guide the Commissioners and practitioners.

Id. at 355 (emphasis in original). The Manual also addresses Code § 64.2-1208, the statute covering fiduciary compensation, which allows compensation in the form of "a reasonable compensation in the form of a commission on receipts or otherwise," unless otherwise provided.

Trotman, as the Manual points out, also set out factors to be considered in making a fee determination; it is proper for a reviewing court to consider the value of the assets, the duration of the work, the difficulties encountered, and the results obtained. 148 Va. at 868-69.

Regarding percentage fees, the courts of the Commonwealth established long ago a general rule that a commission of 5% of receipts is reasonable for an executor. Manual for Commissioners of Accounts at 356 (noting that the "general rule" dates back to 1793); *see, e.g.*, *Granberry's Ex'r v. Granberry*, 1 Va. (1 Wash.) 246, 250 (1793) ("An executor, is certainly entitled to some compensation for his trouble, and that, by custom, is generally fixed at five per cent upon actual receipts."); *Perrow v. Payne*, 203 Va. 17, 25 (1961). While rates exceeding or less than 5% have been employed, where an executor simply distributes personal property in kind, or performs no extraordinary services and assumes no unusual responsibilities, courts have held that 2.5% of the distributed personal property constitutes reasonable compensation. *See Virginia Trust Co. v. Evans*, 193 Va. 425, 434 (1952) (2.5% on stocks delivered in kind); *Koteen v. Bickers*, 163 Va. 676, 691 (1934) (7.5% for "something more than an ordinary executor"); *see also Perrow v. Payne*, 203 Va. 17 (1961) (compiling cases); Manual for Commissioners of Accounts at 356.

Although the defendant in the instant case was not performing the role of an executor in marshaling assets or distributing property pursuant to a will, the above-cited cases are instructive. Here, any "extraordinary circumstances" of which the defendant might try to avail himself were created, for instance, by his rampant trading of a stock fund that originally had a value of approximately $350,000. (*See* Plaintiff's Ex. 7.) Yet as the evidence showed, for example, the defendant made over 2,500 trades and turned the portfolio over approximately 55 times in the year 2013 alone, all to no advantage. (*See* Tr. of 11/17/16 at 41; Tr. of 11/8/16 at 59-65.)

Prior to the March 22, 2017, hearing, the Court considered "Exhibit 11," schedules attached to filed tax returns, proffered by Mr. Larsen following the close of evidence to provide additional support to Plaintiff's Rebuttal Exhibit 3. The defendant objected to admission of the additional records on the basis that such records had not been provided,

as well as on grounds of timeliness and relevancy, which objections the Court sustained. However, defense counsel subsequently indicated, by letter, that the defendants did have in their possession copies of the schedules proffered, but perhaps in a different form, and accordingly withdrew that portion of the objection. The Court found that the proffered records were relevant and admissible, and a part of the submitted 1999 estate tax return, which is part of the attorneys' agreement that all tax returns were stipulated to be admissible. Therefore, Exhibit 11 (two pages) was replaced with Plaintiff's Exhibit 11 A, B, & C, which reflect the three independently admitted financial statements for the relevant years.

However, regarding the fees on the 116 shares of Higgerson-Buchanan stock, the Court finds that there is insufficient evidence regarding whether the value of these shares, represent the entirety of Higgerson-Buchanan's value, or only the 1/3 over which the defendant had a fiduciary responsibility. The defendant claimed that he valued the assets of Higgerson-Buchanan and divided this figure by three to arrive at the value, which coincidentally, was the same value as the 116 shares of stock.[5] Although the Court finds this most recent testimony inapposite to the method described in earlier testimony (*see* Tr. of 11/7/16 at 59-60, 72-73), given the lack of refuting evidence and the fact that the values resulting from both methods were the same, the Court is unable to definitively rule that the defendant improperly valued the Higgerson-Buchanan stock. In any event, Mr. Miller testified that Plaintiff's Exhibit 16 was created by using the defendant's value of the Higgerson-Buchanan stock (Tr. of 11/7/16 at 205), and the Court accepts that exhibit as an accurate reflection of damages.

The fees charged by the defendant (working for a former law firm: Payne, Gates, Farthing, & Radd) for the first seven years of the trust averaged $23,227 per year. Subsequently, the fees increased four and one-half times, when the defendant allegedly used the same fee schedule, increasing the average yearly fee to $104,440. The compensation taken without adequate notice or explanation as to the method and rate as required by Code § 64.2-775(B)(4) likewise violated the defendant's duty of care; Mr. Miller testified that the defendant's invoices did not specify such information for the beneficiary. (Tr. of 11/7/16 at 207-08.)

In order to address the defendant's in-court explanation of how he charged the trust, we must take into account how he addressed compensation in his annual reports. The defendant claimed the fee schedule that he developed with his prior firm was utilized, and if a line item or the schedule did not cover the time that he devoted to a particular aspect of management, he utilized a percentage calculation. (Tr. of 11/7/16 at 113.)

[5] It is apparently from that value that the defendant applied his percentage to arrive at what he felt his fee should be. (*See* Tr. of 11/21/16 at 38.)

The Court sustained the plaintiff's objection to the introduction of the fee schedule itself that the defendant claimed he utilized in his determination of reasonable compensation, but the defendant additionally claimed that his fees were reflected on a series of yellow legal pad pages wherein all calculations were written in red ink. (Defendant's Ex. 3.) The plaintiff objected to these sheets as well on the basis that their facial appearance indicated that they were written *ex post* in a few sittings to create a basis for the defendant's fees, rather than reflecting the records actually kept during his tenure as trustee. The Court, however, overruled that objection.

The Court reviewed Defendant's Exhibit 3, and while the pages are all consistent in condition and the ink and handwriting appear the same, the Court cannot say that they were manufactured for the purposes of trial or reflect copied consolidation of other papers prepared over the years. These reports read as if they address the hours attributable to the work. However, no number of hours is listed and no hourly rate is ever set forth. Although Mr. Miller felt that based on those reports, the defendant was charging by the hour, the defendant specifically denied same. (Tr. of 11/7/16 at 113, 208.)

The defendant testified that the annual reports reflected the amount of work that he performed, which he used to balance against what the fee schedule indicated, and gave him a basis to increase the fee if necessary based on a percentage. (Tr. of 11/7/16 at 113.) When questioned by the Court as to why he even considered a percentage as the basis of the fee when the decedent had specifically requested the defendant to strike the language of the trust allowing a percentage-based fee, the defendant did not have a clear explanation. (Tr. of 11/8/16 at 236-38.)

The Court therefore has before it an undisclosed blended method of charging and an undisclosed rate of pay, and the Court finds that the defendant is in violation of Code § 64.2-775(B)(4), requiring the Court to determine whether the compensation charged in collected by the defendant was reasonable under the circumstances and evidence presented.

The defendant taking a percentage fee of the passive asset — the Higgerson-Buchanan stock of which he represented less than one-third — was overreaching and contrary to the best interests of the trust beneficiary. Additionally, the defendant knew and dealt with the owners of the other two-thirds, attended meetings with them, knew all of the stock was held within the family, and knew that there were no actions taken by the others that would put the percentage he represented at risk. The suggestion that the defendant earned the claimed fees by reviewing some reports, participating in a half-dozen meetings regarding the election of directors and officers (of which he was neither), and suggesting an attorney for an imminent eminent domain action is unavailing.

Therefore, the Court specifically *finds* from the evidence that the defendant violated Code § 64.2-764(A) in that the trusts were not administered solely to the interests of the beneficiaries. The amount of compensation taken by the defendant amounted to 38% of the total distributed to the beneficiary. The trusts at issue were "plain vanilla trusts" as Mr. Miller testified (Tr. of 11/7/16 at 201), and there was no reason for the defendant to assess fees in the amounts that he did.

Damages

Under the circumstances, and assuming that the defendant had the right to take a fee from a portion of the non-traded stagnant stock (Tr. of 11/7/16 at 203-06), which constituted 1/3 value of the company as a whole,[6] resulted in appropriations of $770,471.33 taken by the defendant in excess of the Commissioner of Accounts Guidelines for Fiduciary Compensation, set forth in the Manual. (*See* Tr. of 11/7/16 at 206-07; Plaintiff's Exs. 15 & 16.)

The Court thus finds that the appropriate fee for the defendant's services amounts to $286,746.10, which fairly compensates the fiduciary for his one-sided efforts in handling the trusts, where said fiduciary, for whatever unknown reason, did not feel he had to advise the beneficiary of the breadth of his actions, which violated his duties of care and loyalty. Therefore, the Court awards damages of $770,471.33 (the $1,057,193.48 collected, less the $286,746.10 noted above). (*See* Tr. of 11/7/16 at 206; Plaintiff's Ex. 16; Manual at 363-64.)

<u>Count II: Conversion</u>

It is well settled in the Commonwealth that "the tort of conversion 'encompasses any wrongful exercise or assumption of authority . . . over another's goods, depriving him of their possession; [and any] act of dominion wrongfully exerted over property in denial of the owner's right, or inconsistent with it.'" *PGI, Inc. v. Rathe Prods., Inc.*, 265 Va. 334, 344 (2003) (quoting *United Leasing Corp. v. Thrift Ins. Corp.*, 247 Va. 299, 305 (1994)) (internal quotation marks omitted).

To the extent that the defendant converted the funds of the plaintiff, any recovery for this tort overlaps the above-detailed breaches, and the plaintiff is entitled to no additional damages. *See, e.g.*, *Wilkins v. Peninsula Motor Cars*, 266 Va. 558, 561 (2003) (A "trial court must assure that a verdict, while fully and fairly compensating a plaintiff for loss, does not include duplicative damages.").

[6] While the Court takes no specific position today as to whether a fiduciary can take a percentage fee of stagnant stock assets, it accepts the testimony of Ms. Patterson and Mr. Miller under the circumstances.

Count III: Unjust Enrichment

To recover for unjust enrichment, the plaintiff must prove that: (1) she conferred a benefit on the defendant(s); (2) the defendant(s) knew of the benefit and should reasonably have expected to repay the plaintiff; and (3) the defendant(s) accepted or retained the benefit without paying for its value. *See, e.g., Schmidt v. Household Fin. Corp., II*, 276 Va. 108, 116 (2008).

The Court finds that the evidence in this matter does not establish recovery for unjust enrichment, as the quasi-contractual nature of the claim is inapplicable to the defendant's conduct. *See, e.g., Wells Fargo Bank, N.A. v. Hall*, No. CL16-2867, 2017 Va. Cir. LEXIS 73, at *8 (Chesapeake City 2017). To the extent any such recovery would be appropriate, it would be duplicative of the recovery set forth *supra*. *See Wilkins*, 266 Va. at 561.

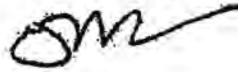
Attorney's Fees

"The general rule in this Commonwealth is that in the absence of a statute or contract to the contrary, a court may not award attorney's fees to the prevailing party." *Prospect Dev. Co. v. Bershader*, 258 Va. 75, 92 (1999). Code § 64.2-795, however, provides: "In a judicial proceeding involving the administration of a trust, the court, as justice and equity may require, may award costs and expenses, including reasonable attorney fees, to any party, to be paid by another party or from the trust that is the subject of the controversy." The Court will therefore reserve the issue of attorney's fees to the prevailing party, requesting that the attorneys set a Wednesday motion date for the Court to address Mr. Larsen's request. The Court asks Mr. Larson to submit the amount of fees requested and the bases therefore, copying Mr. Cales on same, well in advance of the hearing.

CONCLUSION

The Court accordingly finds that the defendant is liable for his breach of the prudent investor rule in the amount of $1,382,653, and excessive fees in the amount of $770,471.33, as well as interest calculated from the last date the defendant performed duties as a fiduciary for the trusts in question. Plaintiff's counsel is requested to prepare an order consistent with this letter opinion, retaining same for entry and endorsement until the conclusion of a hearing regarding attorney's fees.

Yours sincerely,



John W. Brown
Judge

CC: Hon. Carol C. Mayo, Clerk of Court

VIRGINIA: IN THE CIRCUIT COURT FOR THE CITY OF CHESAPEAKE

IVAN L. HIGGERSON SR. & SANDRA BUTT AS CO-EXECUTORS OF THE ESTATE OF EDITH F. HIGGERSON, DECEASED; IVAN L. HIGGERSON, SR. & SANDRA H. BUTT, INDIVIDUALLY, & IVAN L. HIGGERSON, JR., CHRISTIE L. FAULEY, TARA L. GREIFE & LESLIE G. ERICKSON; AND ELIZABETH METTS ALLEN, ESQ., AS TRUSTEE OF THE IVAN HIGGERSON MARITAL TRUST, THE IVAN HIGGERSON FAMILY TRUST, AND THE IRREVOCABLE LIFE INSURANCE TRUST AGREEMENT OF IVAN HIGGERSON,

Plaintiffs,

v. : At Law No. 14-2929

PHILIP R. FARTHING, ESQ., AS THE FORMER TRUSTEE OF THE IVAN HIGGERSON REVOCABLE TRUST AGREEMENT, THE IVAN HIGGERSON MARITAL TRUST, THE IVAN HIGGERSON FAMILY TRUST, AND THE IRREVOCABLE LIFE INSURANCE TRUST AGREEMENT OF IVAN HIGGERSON, PHILIP R. FARTHING, P.C., AND PHILIP R. FARTHING IN HIS INDIVIDUAL CAPACITY,

Defendants.

AMENDED FINAL JUDGMENT ORDER

UPON TRIAL of this matter and upon consideration of the evidence and argument offered by counsel for the parties, it is

ADJUDGED, ORDERED and DECREED that, for the reasons set forth in the Court's Memorandum Opinion dated June 20 2017, which is incorporated herein by reference, the plaintiffs be and hereby are awarded a verdict in amount of TWO MILLION ONE HUNDRED FIFTY-THREE THOUSAND ONE HUNDRED TWENTY FOUR and 33/100 DOLLARS ($2,153,124.33), against the defendants, jointly and severally, with interest at a rate of 6% from May 6, 2015. In addition, the Court has already entered a separate Order dated July 7, 2017, awarding attorney's fees to the plaintiff in the amount of ONE

VSB Exhibit

B

HUNDRED ONE THOUSAND SIXTY-TWO and 50/100 DOLLARS ($101,062.50), which is incorporated as part of this Final Judgment Order.

ENTERED this 28th day of July, 2017.

Judge

I ask for this:

Gregory S. Larsen (VSB 024112)
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Counsel for Plaintiffs

Seen and objected to on the basis that the Court erred in finding a verdict for the plaintiffs and for the reasons stated on the record during trial and based upon the objections stated during trial.

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