

# ACPNS LEGAL CASE REPORTS SERIES

This series compiles short summaries of significant cases involving charitable, philanthropic, nonprofit and social enterprise organisations in Australia and overseas.



## In the Matter of the Otto Bremer Trust

Ramsey County District Court, Minnesota, Court File No. 62-C9-61-315222, Robert Awsumb J, 29 April 2022

Application by a State Attorney General to remove trustees of a charitable trust.

**Key words:** Charitable Trusts, USA, Minnesota, Trustee, Fiduciary Duties, Conflict of Interest, Removal of Trustee

1. In 1944, the Otto Bremer Foundation, now the Otto Bremer Trust (OBT), was established by Otto Bremer with US\$ 2 million in the corpus.
2. OBT is a charitable trust organized under the laws of the State of Minnesota with a formal trust deed that has a wide range of charitable objects. The trustees were initially three individuals (not a corporate trustee) close to the settlor Otto Bremer. The trustees could appoint their successors. The current trustees comprise the third generation of trustees, each with family ties to the initial trustees, and they had made trustee successor appointments of specific relatives if they died or became incapacitated.
3. Otto Bremer was a German immigrant who became a prominent banker and community leader in Minnesota. In the 1920s, he held ownership in more than fifty banks throughout Minnesota, Montana, North Dakota, Wisconsin, and Iowa. In 1943, Bremer created a holding company for his investments in community banks called the Otto Bremer Company, now the Bremer Financial Corporation (BFC). BFC operates as a regional financial institution, and through its wholly owned subsidiary, Bremer Bank, National Association (Bremer Bank). Bremer Bank branches are located in Minnesota, North Dakota and Wisconsin.
4. On his death in 1951, Bremer's residual estate was transferred to the foundation to be used for charitable purposes. The trust corpus exceeded US\$4 million at this time, and has now grown to over US\$2 billion. The vast majority of the value of trust assets consists of ownership of BFC stock, with only about twelve percent, or \$234 million, being non-BFC assets.
5. In the past nine years, the current trustees distributed nearly \$500 million to charities through various charitable programs, with the number of distributions increasing in each successive year from about \$36 million in 2012 to over \$71 million in 2020 in order to meet the IRS requirement to distribute at least 5% of the fair market value of its overall assets.

6. In 2014, the trustees removed the long-time OBT Executive Director and eliminated the position entirely, drawing criticism from other local foundation leaders that OBT was not exhibiting good governance practices. In 2019, the Trustees sold a portion of the shares OBT held in Bremer Bank stock. Bremer Bank leaders saw the sale as a breach of the trustees' fiduciary duties and urged the Attorney General to investigate the OBT trustees' practices. An investigation led to a number of claims being made to the Court by the Minnesota Attorney General (AG).
7. The AG requested the Court to remove the three trustees in response to allegations related to trustees' compensation, general administration, human resources, trust expenses, grant making, and the manner of sale of its BFC stock.
8. The Court reviewed a substantial amount of evidence about the trust and trustees resulting in a judgment of over 100 pages. The Court noted that:
  - Under statute a Court may remove a trustee where they have committed a serious breach of trust, or that removal of the trustee best serves the interest of the beneficiaries because of unfitness, unwillingness, or persistent failure of the trustee to administer the trust effectively; and
  - It decides whether a trustee acts in good faith, from proper motives, and within the bounds of reasonable judgment, to determine whether an abuse of authorized discretion occurred.

#### **Use of the Strategic Grant Making Process**

9. The Court summarised the allegations of the AG as (at [21]):

...that Trustees' use of the strategic grant making process constitutes a breach of their fiduciary duties. They assert that Trustees breached the duty of care, loyalty, and good faith by failing to implement adequate processes and controls over strategic grant-making that were sufficient to protect the Trust. They also argue that Trustees breached the duty of good faith by making grants that were not authorized by the Trust Instrument. Finally, the AGO argues that Trustees breached the duty of loyalty by making strategic grants that constituted conflicts of interests and to further their personal interests.

10. Strategic grants were led by trustees generally, involved larger amounts of money and occurred throughout the year, often made outside of the staff's grant process because of the larger amounts of money, longer term of the grant, and outside the usual staff process and grant parameters.

11. The Court determined that (at [22]):

[T]he use of the strategic grant making process, combined with the responsive process that has historically been used, is within the discretion of the Trustees under the Trust Instrument and does not constitute a breach of their fiduciary duties. Trustees are the ultimate determiners when it comes to making grants. They have established and oversee a professional operation that includes many dedicated staff members to assist them in the process. It would likely be impossible to effectively operate the Trust without the staff's help. Utilizing the strategic process whereby Trustees take personal responsibility for determining larger grants is an

acceptable enhancement to the overall charitable giving process. The Trustees often involve staff members in obtaining an application from the recipient and in vetting the organization and anticipated use of grant money. The strategic process, like the responsive process, requires the same level of scrutiny and approval by the Trustees. The Court rejects the view that the process presently in place is inadequate, improper, or otherwise constitutes a violation of Trustees' fiduciary obligations.

### **Unauthorized Grants**

12. The AG argued that some grants did not technically comply with the Trust and constituted a breach of fiduciary duties. The Court disagreed, explaining that the trustees had broad discretion in interpreting the Trust requirements. The Court concluded that the grants, which complied with the intent (if not the literal reading) of the Trust, did not constitute a breach of trust or fiduciary duty.

### **Conflict of Interest**

13. The AG argued that grants made to nonprofits on whose boards trustees serve violated their duty of loyalty by making grants that constituted conflicts of interests. The Court found that the trustees complied with and disclosed potential conflicts to each other in accord with the stated conflict policy before any vote on a potentially conflicted grant was made.

### **Trustees' Court-Approved Compensation and Investment Advisory Fees**

14. The AG argued that the total amount of compensation paid to the trustees was excessive and unreasonable. The original Trust document explicitly authorized the trustees to compensate themselves for services up to 4% of the cash income of the Trust, to be divided among them as they choose. The trustees' payments never came close to 4% of the cash income of the Trust.

15. The Court had previously approved the trustees' compensation, and methodology for determining it, five times since 2011. The methodology is still currently in use. The trustees paid themselves each a base fee of \$353,307 in 2020. In addition, OBT paid trustees Lipschultz and Reardon an additional \$183,000 and \$191,000 for investment services, respectively.

16. The Court concluded that given the robust previous Court processes and no evidence that trustees hid or misrepresented their compensation in such proceedings there was no breach of trust.

### **Selection of Successor Trustees**

17. The AG argued that furthering trustees' family legacies is not a Trust purpose. If a trustee chose a successor for self-interested motives, as opposed to on the grounds that the successor would serve the interests of the trust, it followed that the appointment was a breach of fiduciary duty.

18. The Court decided that the trustees were free to change the appointments of successors at will. There was no evidence that the appointed individuals were unfit or unable to serve. Only that they were relatives. Further, they would be subject to the requirement of court approval if something happened, and their provisional appointment would then become effective.

### **Trustees' Private Equity Investments Supervised by the Federal Reserve and the Prudent Investor Rule as Modified by the Trust Instrument**

19. The AG argued that the trustees' decision to invest in private investments was a breach of fiduciary duty because banking law made those investments questionable.

20. The Court concluded that in the circumstances of engaging world-class legal and investment advisors and consulting with the Federal Reserve regarding the investments, the trustees' actions were within their authority and did not violate the prudent investor rule.

### **The Sale of BFC Stock Violated the Trustees' Fiduciary Duty**

21. The AG alleged that the trustees' decision to sell a portion of OBT's Bremer Bank stock to a variety of investment banks located outside the state was an abuse of discretion and a breach of the trustees' duty to act in good faith. The AG argued that Otto Bremer's desire was that the shares be retained, except for unforeseen circumstances, and that there be a relationship between BFC and the Trust.

22. The Court noted at the time that the AG was fully informed of the sale and took no objection to it. It was only after the sale was completed that BFC refused to register the buyer's shares and sued the trustees seeking to invalidate the sale that the AG became involved.

23. The Court concluded that trustees' decision to pursue a strategy to further explore options to sell its BFC stock through the sale of the minimum number of shares necessary was not an abuse of their discretion or a breach of trust and did not violate the settlor's intent. To the contrary, under the unique circumstances presented, it was a good faith effort to protect and enhance the Trust.

### **Multiple Breaches of Trust by Lipschultz**

24. The Court found that Lipschultz used OBT assets for personal purposes, including using OBT email to send messages related to his personal business, asking OBT staff to manage his family's calendar and send personal packages.

25. Although these amounts were small in the scheme of the Trust, amounting in total to some several thousand dollars, the Court commented that (at [83]):

In the larger scheme of things, it may be "de minimis." Nonetheless, this misuse of trust assets constitutes self-dealing which is strictly prohibited by law and by the Trust Instrument itself.

26. The Court also found he behaved improperly with the Bremer Bank President and a fellow trustee. Lipschultz also bullied and threatened local nonprofit leaders with the loss of OBT grant funding when the leaders did not support OBT in its disputes with Bremer Bank leaders.

27. The Court recounted that (at [89]):

Some of the most disturbing evidence in this case relates to the actions of Lipschultz in his communications with Junior Achievement's CEO after the conflict with BFC intensified. His actions were based solely on his personal animosity toward BFC and have no place in the charitable community. At worst, his actions could be reasonably interpreted as threats against future grants because Junior Achievement was honoring BFC's board chair. At best it was abusive treatment of a grantee for operational decisions unrelated to any legitimate charitable purpose of the Trust. His behavior caused Junior Achievement to return a \$1.2 million grant, at a most critical time of need.

28. The Court found that Lipschultz should be removed as a trustee, finding that ([91]-[92]):

There is no room in the charitable world for animosity and vindictiveness to infiltrate or impact the decision-making of a charitable trustee. Lipschultz has shown repeatedly that he cannot operate in a purely charitable manner and has allowed his own personal interests, animosity, enmity, or vindictiveness to impact his decisions and behavior as a trustee of one of the region's most important charitable institutions. The Court concludes that Trustee Lipschultz's repeated improprieties constitute a serious breach of trust that justify removal.

29. The two remaining trustees will continue to run OBT subject to a future proceeding to determine whether and how a third trustee will be appointed to replace Lipschultz.

## IMPLICATIONS



This is a judgment which reviews a large amount of evidence concerning the grant making and administration of a large US foundation. It will interest non-American trustees as to what is tolerated by the law in the US and its notion of fiduciary duties.

## VIEW THE CASE



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