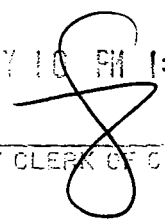


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IN THE SUPERIOR COURT
FOR THE
COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

IN THE MATTER OF THE ESTATE OF)
LARRY LEE HILLBLOM,)
)
Deceased.)

CIVIL ACTION NO. 95-626

**ORDER RE: REPORT OF
THE SPECIAL MASTER**

I. PROCEDURAL BACKGROUND

Prompted by concerns raised by Petitioner Kaelani Kinney and other Claimants to the Estate over actions undertaken by the Executor, Bank of Saipan, the Court solicited the views of Counsel as to the advisability of appointing a Special Master pursuant to Rule 53(b) of the Commonwealth Rules of Civil Procedure. The Court received written submissions from counsel and conducted a hearing on the issue on September 21, 1995. The Court then appointed Rexford C. Kosack, a former Attorney General of the CNMI and, now, a former Special Judge of the CNMI, as Special Master. See, Order dated September 28, 1995. No party objected. That same Order outlined the specific issues referred to the Special Master, and the procedure by which he would conduct hearings and submit a final report to the Court. The five issues for consideration were:

1. What are the relationships of the Bank of Saipan, Joseph Waechter, Commonwealth Holding Corporation, its shareholders, the Carlsmith law firm, DHL Corporation, DHL International,

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1 Deloitte & Touche, and Danao International Holdings to the Estate and to each other as they may affect
2 the Estate?

3 2. What are the different businesses and projects concerning which the Estate must make
4 business decisions or actually operate during this probate?

5 3. How do the persons or business entities identified in the first question relate to the
6 business activities in the second question?

7 4. Are there actual or potential conflicts of interest between the duties that the Bank of
8 Saipan, Joseph Waechter and/or the Carlsmith law firm owe to the Estate and duties they may owe to
9 others?

10 5. Does a review of the Estate's major transactions up to September 28, 1995 indicate
11 that any transaction may have been affected by a conflict of interest or self-dealing involving the
12 Executor?

13 Over the course of four months, the Special Master conducted discovery, held evidentiary
14 hearings, reviewed documents and records, and heard arguments of counsel. On February 22, 1996, the
15 Special Master filed a written transcript of all the proceedings. The following day, February 23, 1996,
16 the Report of the Special Master was filed ("the Report").

17 Pursuant to its September 28, 1995 Order, the Court initially calendared a hearing on the Report
18 for March 13, 1996, requiring all objections or concurrences of interested parties to be filed and served
19 by March 5, 1996 and any reply memorandum of any interested party to be filed and served by March
20 9, 1996. *See* February 27, 1996 Order Calendaring Hearing on Report of the Special Master. However,
21 upon notice that the Deputy Attorney General for the State of California claims to be interested in Mr.
22 Hillblom's estate, and upon the Attorney General's request for an extension of time to file a general
23 appearance in this matter, the Court rescheduled the hearing on the Report to April 1, 1996. All
24 objections or concurrences of interested parties were due March 15, 1996 and any reply memoranda
25 were due March 26, 1996. *See* February 29, 1996 Order Suspending Executor. Given the gravity and
26 complexity of the issues raised in the Report and the fact that the Court could not immediately assess
27 the validity of the Report, the Court suspended the Executor. *Id.* The Court appointed William I.

1 Webster as a temporary Special Administrator to protect and manage the assets of the Estate until the
2 full authority of the Executor is restored or a new executor is appointed in its place. *See* March 22, 1996
3 Order Appointing Special Administrator.

4 A hearing on the Report lasting a full day was held on April 2, 1996. Present at that hearing
5 were: John Osborne, Esq., on behalf of the suspended Executor; Deputy Attorney General for the State
6 of California Yeoryios C. Appallas, Esq., as Representative of the Charitable Beneficiaries under the
7 will; Thomas Scott, Esq., on behalf of Peter J. Donnici, in his capacity as the Chairman of the Board
8 of the Trustees of the Hillblom Charitable Trust; David J. Lujan, Esq. and Joe Hill, Esq. on behalf of
9 Petitioner Kinney, and Randall T. Fennell, Esq. on behalf of Petitioner Moncrieff. All parties present
10 submitted their objections and concurrences to the Report and reply memoranda prior to the hearing and
11 each presented oral argument at the hearing. At the close of the April 2, 1996 hearing, the Court ordered
12 all present to submit their final findings of fact and conclusions of law by April 15, 1996. Satisfied that
13 it has afforded all interested parties ample opportunity to be heard on the subject matter contained in the
14 Report, the Court now renders its final determination on the Report.

15 16 **II. APPLICABLE STANDARD OF REVIEW**

17 In non-jury actions, the court shall accept the Special Master's findings of fact unless clearly
18 erroneous. Com.R.Civ.P. 53(e). The clearly erroneous standard is the same standard that governs
19 appellate review of District Court findings of fact. Fed. R. Civ. P. 52(a); *NLRB v. Sequoia Dist. Council*
20 *of Carpenters*, 568 F.2d 628 (9th Cir. 1977). It applies to findings based on credibility determinations,
21 physical or documentary evidence or inference from other facts. *Anderson v. City of Bessemer City,*
22 *N.C.*, 105 S.Ct. 1504, 1512 (1985). This deferential standard does not entitle a reviewing court to
23 reverse the finding of the trier of fact, even if it is convinced that had it been sitting as the trier of fact
24 it would have weighed the evidence differently. *Id.* at 1507. Rather, "a finding is 'clearly erroneous'
25 when although there is evidence to support it, the reviewing court on the entire evidence is left with the
26 definite impression that a mistake has been committed." *United States v. United States Gypsum Co.*, 333
27 U.S. 364, 395, 68 S.Ct. 525, 542 (1948); *In Re the Estate of Taisakan*, 1 CR 326 (D.N.M.I. App. 1982);

1 *Matagolai v. Pangelinan*, 3 CR 591 (D.N.M.I. 1988); *Aldan v. Kaipat*, 2 CR 190 (D.N.M.I. App. 1985)
2 aff'd 794 F.2d 1371 (9th Cir. 1986) . The party excepting to the Special Master's findings bears the
3 burden of pointing out specifically where findings are clearly erroneous. *NLRB v. Sequioa, supra*.
4 Where there are two permissible views of the evidence, the fact-finder's choice between them cannot
5 be clearly erroneous. *Anderson, supra*, citing *United States v. Yellow Cab Co.*, 70 S.Ct. 177, 179 (1949);
6 *Inwood Laboratories, Inc. v. Ives Laboratories, Inc.*, 102 S.Ct. 2182, 72 (19 82).

8 III. ADOPTION OF FINDINGS OF FACT

9 Petitioners Kinney and Moncrieff concur with the Special Master's findings of fact. *See*
10 Petitioner Kinney's Concurrence With and Comments on Special Master's Report and
11 Recommendations on Appropriate Remedies, dated March 15, 1996 ("Kinney's Concurrence");
12 Petitioner Moncrieff's Concurrence in the Report of the Special Master, dated March 15, 1996
13 ("Moncrieff's Concurrence"). The Executor "disagrees with the general content, tone, speculation and
14 conclusions of the Special Master contained in the Report." Executor's Comments and Objections to
15 Report of the Special Master, dated March 15, 1996, p. 4 ("Executor's Objections"). Yet, the Executor
16 takes no exception to the testimony or documents produced as evidence during the Special Master
17 proceedings. Indeed, the Executor adopts the same transcript of testimony relied upon by the Special
18 Master as "uncontroverted" (*Id.* at 1, 3, 5, 11, 14), but proposes alternative conclusions to be drawn
19 from the facts. *Id.* at 5 ("The Executor will set forth the facts as produced during the proceeding along
20 with its comments and *how these facts should be viewed.*" emphasis added). For example, the Executor
21 concedes its intent to gain control of the Estate by creating Commonwealth Holding Corporation
22 ("CHC") to purchase Bank of Saipan's treasury stock. *Id.* at 9-10. But, it objects to the inference drawn
23 by the Special Master as to the motive behind the transaction, stating that "...the Special Master's
24 speculation that there were other motives of these individuals in connection with these transactions is
25 not based on any of the evidence." *Id.* at 22.

26 Likewise, the Charitable Trust makes no specific objections to facts produced during the Special
27 Master Proceedings and adopts the transcript of testimony and documentary evidence as

1 uncontroverted.^{1/} See generally Opening Comments of the Charitable Trust on the Special Master's
2 Report, dated March 15, 1996 ("Charitable Trust Comments"). Instead, the Charitable Trust objects to
3 inferences drawn by the Special Master from uncontroverted facts. See e.g. *Id.* at 22 ("The Report
4 asserts that the Will Beneficiaries 'are well positioned to influence the outcome of [the DHL-related]
5 claims' (p.114), that they 'seek to continue to influence [the Executor's] actions (p.179), and that pages
6 178-181 of the Report explain 'how [the] Inventory is clearly the product of CHC's control over the
7 Bank.' (p.135). None of this is true.") The Deputy Attorney General for the State of California makes
8 no objections to the evidence produced during the Special Master Proceedings. See generally, California
9 Attorney General's Comments re: Report of the Special Master, dated March 14, 1996.

10 The Special Master reported the circumstances surrounding the major transactions of the Estate
11 in sections I-III, pp. 1-74 of the Report. In addition, the Special Master itemized the undisputed facts
12 upon which his findings are based. See Report, pp. 97-100; 128-29; 137-38; 143-44; 149-50; 175-76;
13 178-79; 181;185; 186-87. The Court recognizes the superiority of the Special Master's position to
14 consider credibility of witnesses and draw inferences from the testimonial evidence. *Anderson, supra.*
15 Neither the Executor, the Charitable Trust, nor the Charitable Beneficiaries makes specific objections
16 to any of the facts contained in the Report. Having examined the record in light of the appropriately
17 deferential standard, the Court finds that these facts are not clearly erroneous. Therefore, the Court now
18 adopts the Special Master's Findings of Fact.

19 20 IV. THE APPLICABLE LAW

21 Findings may be clearly erroneous when they are based on an erroneous view of the law. *Ritter*
22 *v. Morton*, 513 F.2d 942 (1975), cert den 96 S.Ct. 362, reh den 96 S.Ct. 869. The Executor, the
23 Charitable Trust and the Charitable Beneficiaries all assert that the Special Master incorrectly interpreted

24
25 ^{1/} The Charitable Trust did object to the Special Master's exclusion of the Affidavit of Stephen J.
26 Schwartz, sworn to on March 13, 1996, and an expired Agreement between Msrs. Hillblom, Allen,
27 Robinson and Chung, dated January 15, 1982 from the record, (Charitable Trust Comments, Exhibits
28 A and B, respectively). Over Petitioner Kinney's objection, the Court admitted these documents into
evidence at the April 2, 1996 hearing. The Court has reviewed these documents in their entirety.

1 the Executor's fiduciary duty of loyalty by assuming that the duty is owed to the pretermitted heir
2 claimants. *See* Executor's Objections at 53 ("The Special Master incorrectly applies an inappropriate
3 duty of loyalty."); Charitable Trust Comments at 3 ("the Report is based on an incorrect interpretation
4 of fundamental probate law. . ."); Attorney General's Comments at 17 ("the Report is fundamentally
5 flawed by the unsupported assumption that the Claimants are 'beneficiaries,' to whom the Executor
6 owes a fiduciary duty.") These parties further argue that this legal principle permeates the Report,
7 invalidating the conclusions contained therein. *See. e.g.* Charitable Trust Comments at 7, 9 ("the report
8 is inextricably founded on this erroneous proposition.") Finally, the Executor and Charitable Trust urge
9 the Court to reserve judgment on the Report of the Special Master until the Commonwealth Supreme
10 Court determines the parties to whom the Executor owes a fiduciary duty.^{2/} Executor's Objections at
11 54 ("The Special Master's Report should not be accepted until the appeal currently pending . . . is
12 decided by the Supreme Court); Charitable Trust Comments at 7 ("Given the Appeal now before the
13 Supreme Court, it would seem prudent to stay action on the Report until the Supreme Court can give
14 the appropriate guidance on this issue. . .").

16 **A. Fiduciary Duties of the Executor**

17 The Commonwealth Probate Code is silent as to the fiduciary duties of executors. Hence, the
18 Court must look to "the rules of common law, as expressed in the restatements of the law approved by
19 the American Law Institute" 7 CMC § 3401. The RESTATEMENT (SECOND) OF TRUSTS is approved by
20 the American Law Institute and it sets forth the fiduciary duties of trustees. Section 170, in particular,
21 addresses the duty of loyalty of an executor. Section 170 comment "a" specifically states that "The
22 principle stated in this Section is applicable not only to trustees but to other fiduciaries." The Court
23 finds that the RESTATEMENT (SECOND) OF TRUSTS §170 is the applicable standard to determine whether
24 the Executor breached or fulfilled its fiduciary duties.

26 ^{2/} By Order dated January 24, 1996, this Court determined that the Executor's fiduciary duty extends
27 to the pretermitted heir claimants. The Executor filed a Notice of Appeal from that Order on February
28 9, 1995 and the Charitable Trust joined in the appeal.

1 Section 170 provides:

2 §170 Duty of Loyalty

3 (1) The trustee is under a duty to the beneficiary to administer the trust solely in the interest of
4 the beneficiary...

5 The comments to §170 apply this general principle to specific situations, providing examples of
6 what constitutes a breach of the duty. The most significant comments include the following:

- 7 • Comment “b,” stating that the trustee cannot sell trust property to himself, regardless of his good
8 faith or whether he paid fair consideration;
- 9 • Comment “c,” stating that the trustee violates the duty if he sells property to another and he has
10 a personal interest in the sale (e.g. to a corporation in which he has a controlling or substantial
11 interest);
- 12 • Comment “d,” stating that a corporate trustee (like the Bank of Saipan) cannot sell trust property
13 to another of its departments or to a corporation owned by shareholders of the corporate trustee;
- 14 • Comment “e,” prohibiting the sale of trust property to a third person with the understanding that
15 it will be held for the trustee or reconveyed to the trustee;
- 16 • Comment “h,” prohibiting the trustee from selling property in which he has an interest to the
17 trust regardless of good faith or fair consideration;
- 18 • Comment “i,” stating that the corporate trustee cannot sell property to the trust from one of its
19 other departments;
- 20 • Comment “j,” prohibiting the trustee from purchasing an interest in the subject matter of the
21 trust;
- 22 • Comment “l,” prohibiting the trustee from using trust property for his own purposes (e.g. lending
23 money or leasing property to himself);
- 24 • Comment “m,” prohibiting the bank trustee from depositing trust funds into its own banking
25 department;
- 26 • Comment “n,” prohibiting the corporate trustee from selling its own stock to the trust;
- 27 • Comment “p,” prohibiting the trustee from competing with the interest of the beneficiary;

- 1 • Comment “q,” stating that a trustee is under a duty not to be guided by the interest of any third
- 2 person;
- 3 • Comment “r,” broadly prohibiting the trustee from entering into transactions which involve a
- 4 conflict of interest that prevent fair dealing;
- 5 • Comment “s,” prohibiting the trustee from disclosing information learned while acting as trustee
- 6 where disclosure would be harmful; and
- 7 • Comment “t,” broadly prohibiting the trustee from acting in bad faith.

8 The Report includes a detailed analysis of the Executor’s fiduciary duty (pp. 85-93) and states
9 that “...the duty of loyalty of an Executor is found at RESTATEMENT (SECOND) OF TRUSTS §170. Section
10 170 is the substantive law which prohibits self-dealing and a conflict of interest for CNMI executors.”
11 Because it is clear that the Special Master applied the Restatement to the undisputed facts, the Court
12 further finds that the assertion that his findings and conclusions flow directly from the one legal
13 principle currently on appeal before the Supreme Court is misguided. Assuming *arguendo* that the legal
14 principle is incorrect, the Court finds independent support for the Special Master’s findings and
15 conclusions in the Restatement.

16
17 **B. Burden of Proof**

18 The Special Master employed a shifting burden of proof to determine whether the Executor
19 breached its fiduciary duties owed to the Estate, based on the loyalty rule stated in *Fulton National Bank*
20 *v. Tate*, 363 F.2d. 562 (1966). Report at 93-97. Specifically, the burden of proof was placed on
21 Petitioner Kinney to show that the Executor allowed itself to be placed in a position of conflicting
22 loyalties. Upon Petitioner Kinney’s meeting that burden, the burden then shifted to the Executor to
23 disprove that showing or to impose a defense.

24 The Executor objects to the Special Master’s reliance on *Fulton*, asserting that the case is “only
25 applicable in a jurisdiction in which strict liability for breach of fiduciary duties is the standard.”
26 Executor’s objections at 2. However, the Executor concedes that the *Fulton* case addresses the
27 preliminary issue of burden of proof as to whether a conflict is shown to exist. *Id.* at 56, n.16. Upon

1 adopting the shifting burden of proof, the Special Master expressly limited his reliance on *Fulton* and
2 stated that the Report does not address what the burden should be in measuring damages. Report at 96.
3 The Court finds that the Special Master’s limited reliance on *Fulton* and application of a shifting burden
4 of proof was appropriate.

5
6 **V. CONCLUSIONS RE: SPECIAL MASTER REPORT**

7 Applying the RESTATEMENT (SECOND) OF TRUSTS § 170 to the facts stated in the Report, the
8 Court concludes as follows:

9 1. The Executor participated in a plan to take control of the Estate and its administration
10 by a group of claimants and potential beneficiaries. This violates the Executor’s fiduciary duty not to
11 favor one set of beneficiaries over another.^{3/} RESTATEMENT (SECOND) OF TRUSTS §170(q) (“The trustee
12 is under a duty to the beneficiary in administering the trust not to be guided by the interest of a third
13 person.”).

14 2. The Executor improperly delegated the negotiation of the DHL loans to Donnici, a
15 member of the group of claimants, an attorney employed by DHL and a director of DHLI. He did so
16 because of his trust in Donnici as a friend, despite the fact that Donnici had numerous conflicts of
17 interest in handling a transaction between the Estate and DHL. The Executor signed the DHLI loan
18 Agreement on July 18, and the DHLC Loan Agreement on July 25, both of which had been negotiated
19 by Donnici. The Agreements make the Estate a party to the earlier Shareholders’ Agreements and grant
20 the DHL companies valuable purchase rights to the Estate’s DHL stock, its most valuable asset.^{4/} *Id.*

21
22
23 ^{3/} The Charitable Trust asserts that this conclusion in particular is based on the incorrect premise that
24 the Executor owes a duty of loyalty to the pretermitted heir claimants. Charitable Trust Comments at
25 7 (“in fact, [the erroneous proposition]...constitutes the lead point of the Conclusion Section.”). Given
26 the undisputed facts stated in the Report, the Court finds ample support in §170(q) of the Restatement
27 to conclude that the Executor breached its fiduciary duty by participating in a plan to take control of the
28 Estate and its administration.

^{4/} With regard to this conclusion, the Special Master states, and the Court finds, that nothing
contained in the Report should affect the claims of DHLI and DHLC. Report at 157.

